IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

No. 76-742

In the Matter of:

PINE GATE ASSOCIATES, LTD.,

Debtor,

GREAT NATIONAL LIFE INSURANCE COMPANY, formerly USLIFE LIFE INSURANCE COMPANY OF TEXAS, and ALL AMERICAN LIFE AND CASUALTY COMPANY,

Petitioners,

vs.

PINE GATE ASSOCIATES, LTD.,

Respondent.

MOTION FOR LEAVE TO FILE PETITION FOR WRIT OF PROHIBITION AND/OR MANDAMUS AND/OR CERTIORARI TO THE DISTRICT COURT, NORTHERN DISTRICT OF GEORGIA, ATLANTA DIVISION.

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MOTION FOR LEAVE TO FILE PETITION FOR WRIT OF PROHIBITION AND/OR MANDAMUS AND/OR CERTIORARI TO THE DISTRICT COURT, NORTHERN DISTRICT OF GEORGIA, ATLANTA DIVISION.

Petitioners GREAT NATIONAL LIFE INSURANCE COMPANY and ALL AMERICAN LIFE AND CASUALTY COMPANY respectfully move this Court for leave to file the annexed Petition for Writ of Prohibition and/or Mandamus and/or Certiorari, under Section 1651 of Title 28 of the United States Code, directed to the United States District Court for the Northern District of Georgia, Atlanta Division, and to the Honorable William L. Norton, Jr., Bankruptcy Judge

of the United States District Court for the Northern District of Georgia, Atlanta Division. In the event 28 U.S.C. § 2403 is applicable, Petitioners are serving a copy of the within Motion on the Solicitor General, Department of Justice, Washington, D.C. 20530. No Court has made a certification to the Attorney General pursuant to 28 U.S.C. § 2403.

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PETITION FOR WRIT OF PROHIBITION AND/OR MANDAMUS AND/OR CERTIORARI TO THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF GEORGIA, ATLANTA DIVISION.

Petitioners pray that Writs of Prohibition and/or Mandamus and/or Certiorari issue to the United States District Court for the Northern District of Georgia, Atlanta Division, to prohibit the taking of their property without just compensation, to require the provision of adequate safeguards to protect Petitioners against the uncompensated taking of their property, and to review the Orders of Bankruptcy Judge William L. Norton, Jr. denying Petitioners any form of protection or relief and the Orders of District Judge William C. O'Kelley, affirming Judge Norton's Orders.

ORDERS AND OPINIONS BELOW

The Order of Bankruptcy Judge Norton, denying Petitioners' motions for security to indemnify them from damage suffered by reason of the continuance of the automatic stay against lien foreclosure, sequestration for their benefit of the rents, issues and profits of the Pine Gate Apartments, and other relief, is annexed hereto as Appendix E.

A copy of the Order of the United States District Court, Judge O'Kelley, affirming the above order, is annexed hereto as Appendix F.

A copy of the Order of Bankruptcy, Judge Norton, dated June 30, 1976, denying Petitioners any and all relief requested in their complaint for relief from the injunction and automatic stay under Bankruptcy Rule 12-43(a) and to sequester rents, issues and profits is annexed hereto as Appendix H.

A copy of the Order of the United States District Court, Judge O'Kelley, affirming the above order, is annexed hereto as Exhibit I.

A copy of the Order of Bankruptcy, Judge Norton, dated dated October 14, 1976, allowing the taking of Petitioners' security without full payment of the debt secured thereby, directing Petitioners and Respondent to present evidence as to the value of said security and "to show cause" "what amount the Debtor must pay" therefore, is annexed hereto as Appendix A.

JURISDICTION

The jurisdiction of this Court is invoked pursuant to the provisions of Title 28, United States Code, Section 1651(a), which provides that this Court "may issue all writs necessary or appropriate" in aid of its jurisdiction agreeable to the uses and principles of law.

QUESTIONS PRESENTED

1. Are creditors secured by interests in real property entitled to any protection against damages caused by the imposition and maintenance of the stay against lien enforcement imposed automatically upon the mere filing of a petition under Chapter XII of the Bankruptcy Act?

2. Is a secured creditor's right to due process violated by the imposition of a stay against lien enforcement where that stay is imposed without:

   a. notice;

   b. opportunity to be heard;

   c. prior judicial approval or scrutiny; and

   d. bond or other form of protection against damages caused by the stay?

3. May a secured creditor's interest in real property be taken, under Section 461(11) of the Bankruptcy Act, without repaying the debt secured by that property?

4. If so, is the secured creditor adequately protected by the availability of a claim for damages against the United States under the Tucker Act?

5. Does a plan which reduces a secured creditor's debt in order to pay subordinate creditors accord the secured creditor equal protection of the law?

6. Is such a plan "in the best interest of creditors" when the secured creditor is owed more than 90% of the Chapter XII debtor's debts?

7. May this Court constitutionally legislate changes in the Bankruptcy Act under the delegated power to prescribe rules of Bankruptcy procedure?

CONSTITUTIONAL PROVISIONS, STATUTES AND RULES INVOLVED

Constitutional Provisions

1. The Fifth Amendment to the Constitution of the United States provides in pertinent part as follows:

> "No person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

The following are set out in Appendix A.

2. Article I, Section 1 of the Constitution.
3. Article I, Section 8 of the Constitution.
4. Article III, Section 1 of the Constitution.

Federal Statutes & Rules of Civil Procedure

1. Title 28 U.S.C. § 2075.
2. Federal Rules of Civil Procedure, § 65(1).
3. Tucker Act, 28 U.S.C. § 1491.

Bankruptcy Act Provisions

1. Bankruptcy Act, Chapter XII, Real Property Arrangements By Persons Other Than Corporations, States Code, Title 11, Chapter 12, §§ 801-926:

   A. 11 U.S.C. § 861(11)(c).

   B. 11 U.S.C. § 828.

   C. 11 U.S.C. § 823.

   D. 11 U.S.C. § 806(9).

Rules of Bankruptcy Procedure

1. Rules of Bankruptcy Procedure, Rule 12-43(a), (e).
2. Rules of Bankruptcy Procedure, Rule 12-36.
3. Rules of Bankruptcy Procedure, Rule 12-17(b).

STATEMENT OF THE CASE

This case is a result of the Rules of Bankruptcy Procedure, promulgated by this Court, which abdicate to private individuals the discretion to impose the injunctive powers of the United States.

In June, 1973, Petitioners loaned a combined total of $1,380,000 to Respondent Pinegate Associates, Ltd. Pinegate is a Georgia limited partnership formed to purchase and own a 118-unit, two-story apartment complex outside of Atlanta, Georgia. The loans were evidenced by two Security Deed Notes,[a] which were collateralized by a Security Deed and Security Agreement[b] encumbering the real property, together with an Assignment of Leases and Rents.[c]

Respondent is what is commonly known as a "tax shelter".[d]

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[a]Appendix B.

[b]Appendix C.

[c]Appendix D.

[d]"The general objective of the Partnership is to purchase and own a 118-unit two-story garden apartment complex presently being completed by Beaver Ruin Associates Inc. and Mr. W. Daniel Faulk, Jr., on Beaver Ruin Road, Norcross, Gwinnett County, Georgia.

The Partnership investment objectives are to provide a return on investment derived in three principal ways. First, a return is sought from cash flow generated from rentals, such rentals may be escalated periodically with the rising inflationary trends. Additional yield is to be derived from tax losses generated from the operation of the project and the manner in which investments are made. Such losses may be substantially in excess of the amount of cash invested and are available to offset against taxable income of Limited Partners from other sources for federal income tax purposes, and under certain circumstances for state and local income tax purposes as well.

The present mortgages are being amortized and the property appears to be well located to take advantage of the increasing values occurring as Atlanta expands further into Gwinnett County. These additional factors lead to the expectation, though speculative, that the property can be sold or refinanced in the future at a price greater than the Partnership cost." — *Proposal for Investment in Pinegate Associates*

Respondent defaulted in the performance of its obligations under the terms of the Security Deed and Security Agreement by failing to make payments of all installments of principal and interest due August 1, 1975 and thereafter, and by failing to pay real property taxes for the year 1975.

The Security Deed and Security Agreement grants Petitioners the right to foreclose nonjudicially, in accordance with the provisions of Georgia law. Petitioners have been prevented from exercising this remedy at all times since December 23, 1975, when Respondent filed its petition under Chapter XII of the Bankruptcy Act[e] in the District Court of the Northern District of Georgia, Atlanta Division. Contrary to law, but in accordance with the Rules of Bankruptcy Procedure promulgated by this Court, the petition was not accompanied by any plan of arrangement.

During the period beginning with Respondent's default and ending with the petition, Respondent repaid loans to its General Partner in an amount in excess of $27,000.

Upon the filing of Respondent's petition, Petitioners were *automatically* enjoined from conducting a foreclosure sale. Under Georgia law, foreclosure sales may be held on the first Tuesday of any month, the same having been duly advertised the previous month. But for the automatic stay, Petitioners would have been able to cause a foreclosure sale to be held February 3, 1976 and at that sale would have been entitled to either buy the property or receive the proceeds of a sale to another bidder, thereby either owning the property formerly securing the loan or realizing the market price available February 3, 1976, to repay their loan.

Respondent has not been required to post any form of security to protect Petitioners from their losses caused by the injunction, nor has it been required to pay anything for

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[e]11 U.S.C § 801, *et seq.*

its use and occupation of the property. Petitioners' motion to sequester the rents, issues and profits subject to their Assignment of Leases and Rents was denied.[f] On appeal to the District Court, the Order was affirmed.[g]

The apartment complex subject to Petitioners' security interest represents virtually the sole asset of Respondent. Pinegate's schedules show the value of its real property to be slightly more than 99% of its assets.[h]

Conversely, the encumbrances against that property represented, at filing, practically all the Respondent's debt[i] — and that proportion has continued to increase for nearly a year.

The essence of the Chapter XII proceeding, therefore, is a proceeding wherein one party has invoked the powers of the court to escape its obligations to the other — first by obtaining the automatic injunction against foreclosure, and now, as explained below, by attempting to take Petitioners' property at a Bankruptcy Court-authorized discount.

On January 13, 1976, Petitioners filed a complaint seeking relief from the automatic stay and seeking an order sequestering the rents, issues and profits. Oral arguments were heard on February 17, resulting in the Order refusing

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[f]Bankruptcy Court Order, Appendix E.

[g]District Court Order, Appendix F.

[h]Appendix G. Pinegate lists assets of $1,999,377.54, of which $1,981,280 is claimed to be the value of the real property.

[i]Total liabilities are listed as $1,601,925.50. Petitioners' debt is listed as $1,353,426.15 and unpaid property taxes, prior to Petitioners' lien, is listed as $21,459.55. The remaining "debt" listed includes $138,000 owed to another of Respondent's General Partner's enterprises and represents the agreed-upon purchase price of the land and $6,000 in past due rent. Of the $28,500.36 listed as unsecured debt, $11,630.84 is owed to the General Partner.

to grant any of the relief requested (Appendix E). This order was appealed to the District Court, where it was affirmed (Appendix F).

Trial on Petitioners' complaint was had on April 1, 5 and 20, 1976 and resulted in the order appended hereto as Appendix H, denying Petitioners any and all relief requested in their complaint. Without granting hearing, the District Court made the order, dated November 11, 1976, appended hereto as Appendix I. This order affirms the Bankruptcy Court's order, although the District Court failed to consider the trial being appealed from, apparently under the impression that its pretrial order (Appendix F) covered the point.

Respondent, meanwhile, presented its plan of arrangement on May 14, 1976 and a hearing on confirmation was held May 27, 1976. The proposed plan is appended hereto as Appendix J. The proposed plan is to pay Class I creditors (Petitioners) 1.2 million dollars in full satisfaction of their debts (which are now in excess of 1.5 million dollars); 75% to the second mortgagee; a $120,000 note, payable from operations of the apartment project to Class III creditors (the General Partner's other venture); $2,000 each to members of Class IV; 50% to unsecured creditors (including Respondent's General Partner); and the full amount of priority claims. Adequate protection is to be provided for non-assenting classes by "one of the methods" set forth in § 461.[j] The arrangement is to be executed by selling or refinancing the project and by utilizing accumulated operating income.

Petitioners did not approve the plan. The remaining five classes did.

Respondent has proposed a procedure — purportedly authorized by § 461(11)(c) — whereby the court may appraise the value of Petitioners' security and, upon pay-

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[j]11 U.S.C. § 861. See Appendix A.

ment of the amount thus determined, discharge the indebtedness, and take Petitioners' lien. This is commonly known as the "cram down."

By his opinion dated October 14, 1976, Bankruptcy Judge Norton has determined to follow this procedure. The opinion is appended as Appendix K.

Petitioners have argued below that, absent the protection of some form of security to compensate them for damages caused by the stay against lien foreclosure, Rule 12-43(a) operates to unconstitutionally take their property without just compensation because Respondent, being insolvent, cannot be made to be financially responsible. Petitioners have further argued that the injunction, imposed without notice or opportunity to be heard, violated their right to due process.

The threatened imposition of the "cram down" in the manner stated by the Bankruptcy Court guarantees the certainty of loss to Petitioners — not only of interest from August 1, 1975, not only of the cost to Petitioners of the money the Bankruptcy Court has allowed Respondent to retain and, in effect, finance the Chapter XII proceedings with — but of part of the loan principal itself!

Real estate construction and finance in this country is a multi-billion dollar industry currently in a severely depressed state. One cardinal tenet of the industry is that secured loans are less risky and may therefore be acceptable at lower rates of return. The real property stands behind the obligation, and relatively efficient and economical means, often outside the judicial process, are provided by state laws to realize upon that security. These assumptions are severely jeopardized by the abusive use of the injunctive powers of the United States, through the automatic stay made indiscriminately available in bankruptcy, and are utterly destroyed by the concept sought to be invoked herein by Bankruptcy Judge Norton.

The lending community needs to know whether lenders' property may be taken without just compensation, as Judge Norton proposes, and whether there is, in short, to be any such thing as a secured loan in this country (other than government-insured loans). If not, lenders will have to re-evaluate their policies, raising the return on loans to the level generally applicable to unsecured loans, reducing the loan-to-value ratios (from 75% to perhaps 30-40%), employing some combination of the two — or, perhaps, refusing to make mortgage loans entirely. Many lenders, especially pension funds, Real Estate Investment Trusts, mutual savings organizations, Life Insurance Companies and other publicly owned entities, simply cannot tolerate the inability to underwrite the risk of real estate lending with which they are now faced.

If their property may constitutionally be taken from them, as here threatened, they must know. If not, the bankruptcy lawyers and judges must know.

This matter is of critical importance to the industry and to the national economy. There are nearly a thousand Chapter XII proceedings, tying up billions of dollars of capital, currently pending throughout the country.[k]

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[k]Between January 1, 1975 and November 1, 1976, there were actually 43 Chapter XII proceedings filed in the Northern District of Georgia, Atlanta Division, including the instant case. Fifteen of these were filed between July 1, 1976 and November 1, 1976. These cases are listed in Appendix L. A review of the available information from these files shows that the average amount of secured creditors' claims in the proceedings is approximately $6,000,000, including Colony Square (#B75-3523) in which the claims total in excess of $80,000,000, and approximately $2,500,000, excluding Colony Square. If these averages are projected nationally to the over 850 such proceedings referred to by Judge Norton in footnote 12, page 7 of his Opinion (Appendix K), the dollar volume of mortgage loans currently being directly affected by such proceedings is somewhere between 3 billion and 6 billion dollars. There may well be an even greater amount of capital tied up in Chapter XI proceedings.

Petitioners therefore seek extraordinary relief in this Court to prohibit the taking of their property by means of the threatened imposition of the "cram down;" to require that the automatic stay be conditioned upon the provision of adequate safeguards to protect Petitioners from losses caused by the stay; and to require the sequestration of the property's rents, issues and profits for Petitioners' benefit and/or the payment to Petitioners of the reasonable rental value of the project from August 1, 1975 until such time as the Chapter XII proceedings are terminated or Petitioners are able to foreclose.

SUMMARY OF REASONS FOR GRANTING THE WRIT

This Court has the power to issue the common law writs of prohibition, mandamus and certiorari, and may do so directly to the District Court. 28 U.S.C. § 1651(a); *Ex Parte Republic of Peru,* 318 U.S. 578, 63 S. Ct. 793, 87 L. Ed. 1014 (1943); *Los Angeles Brush Mfg. Corp. v. James,* 272 U.S. 701, 47 S. Ct. 286, 71 L. Ed. 481 (1927); *McCullough v. Cosgrave,* 309 U.S. 634, 60 S. Ct. 703, 84 L. Ed. 992 (1940); *Ex Parte United States,* 287 U.S. 241, 53 S. Ct. 129, 77 L. Ed. 383 (1932).

The question of whether the writ(s) shall issue is directed to the discretion of the Court. *Ex Parte Peru, supra.* That discretion should be exercised where, as here, the following conditions obtain:

1. Where the constitutionality of Rules promulgated by this Court must be decided. *Los Angeles Brush Mfg. Corp. v. James, supra; McCullough v. Cosgrave, supra; LaBuy v. Howes Leather Co.,* 352 U.S. 249, 77 S. Ct. 309,1 L. Ed. 2d. 290 (1957), *reh. den.,* 352 U.S. 1019, 77 S. Ct. 553, 1 L. Ed. 2d. 560 (1957); *Schlagenhauf v. Holder,* 379 U.S. 104, 85 S. Ct. 234, 13 L. Ed. 2d. 152 (1964);

2. Where a question of great public importance is involved. *Ex Parte United States, supra; LaBuy v. Howes Leather Corp., supra.*

3. Where appeal is an inadequate remedy, or there is no other remedy. *Los Angeles Brush Mfg. v. James, supra; DeBeers Consol. Mines v. U.S.,* 325 U.S. 212, 65 S. Ct. 1130, 89 L. Ed. 1566 (1945); *Ex Parte United States, supra; United States Alkali Export Ass'n, Inc. v. U.S.,* 325 U.S. 196, 65 S. Ct. 1120, 89 L. Ed. 1554 (1945).

Petitioners assert that *all* of the above considerations are present in this case, because it concerns the validity of the Rules of Bankruptcy Procedure and their effect upon the credit market of the nation. Petitioners assert that the Chapter XII Rules, as applied, take their property without due process or just compensation and that that taking is a constant erosion, precluding the utilization of the appellate process as a remedy.

The Chapter XII Rules, substantially changing the entrance requirements into Chapter XII, have opened the door to abuse. In making Chapter XII more accessible, they have handed over the injunctive power of the United States, since the mere filing of a Chapter XII petition results in an automatic stay of any action to enforce a lien. The Rules have transformed Chapter XII from a rigorous, expedited procedure wherein a debtor and his creditors may quickly determine whether an acceptable plan is possible to an instrument of oppression and delay.

While Congress may delegate the power to make rules of procedure to this Court, Congress has not — and cannot — delegate the power to drastically alter the Bankruptcy Act. Rules of Bankruptcy Procedure may not repeal Acts of Congress.

The automatic stay against lien enforcement operates to take property from the foreclosing secured creditor without notice, opportunity to be heard, prior judicial approval or scrutiny, or any form of protection against loss, thus violating the creditor's right to due process. *Sniadach v. Family Finance Corp. of Bay View,* 395 U.S. 337, 89 S. Ct. 1820, 23 L. Ed. 349 (1969); *Fuentes v. Shevin,* 407 U.S. 67, 92 S. Ct. 1983, 32 L. Ed. 2d. 556 (1972) *reh. den.* 409 U.S. 902, 93 S. Ct. 177, 34 L. Ed. 2d. 165 (1972); *Goldberg v. Kelley,* 397 U.S. 244, 90 S. Ct. 1011, 25 L. Ed. 2d. 287 (1970); *North Georgia Finishing, Inc. v. Di-Chem, Inc.,* 419 U.S. 601, 95 S. Ct. 719, 42 L. Ed. 2d. 751 (1974); *Mitchell v. W.T. Grant Co.,* 416 U.S. 600, 94 S. Ct. 1895, 40 L. Ed. 2d. 406 (1974); *Boddie v. Connecticut,* 401 U.S. 371, 91 S. Ct. 780, 28 L. Ed. 2d. 113 (1971).

The automatic stay operates to take the secured creditor's property because no protection is provided against the continuous erosion taking caused by the passage of time during the period of the injunction. Without any such protection, there is no source available to pay the interest and taxes which continue to accrue, since the debtor is insolvent. The stay permits the debtor to incur *new* debts without any responsibility for their payment. Additionally, many lenders must continue to pay others for funds they have loaned to the debtor and are precluded from collecting. There are no safeguards provided to insure just compensation. The stay, therefore, as applied, violates the Fifth Amendment. *Louisville Joint Stock Land Bank v. Radford,* 295 U.S. 555, 55 S. Ct. 854, 79 L. Ed. 1593 (1935); *W. B. Worthen v. Kavanaugh,* 295 U.S. 56, 55 S. Ct. 555, 79 L. Ed. 1298.

Where a moratorium against lien enforcement is justified by an emergency situation, safeguards must be provided for the creditor. *Radford, supra; see Home Building & Loan*

Ass'n v. Blaisdell, 290 U.S. 398, 54 S. Ct. 231, 78 L. Ed. 413 (1934); *East New York Bank v. Hahn,* 326 U.S. 23, 66 S. Ct. 69, 90 L. Ed. 34 (1945). The latter three cases resulted from legislative efforts to relieve farmers from the effects of the depression, where their plight was considered to comprise a national emergency. No such emergency exists requiring extraordinary steps to protect tax-shelter speculative ventures such as that of Respondent herein.

Petitioners have not consented to Respondent's plan. The other classes of creditors, comprising less than 10% of the amount of Respondent's debts, have approved the plan. This small minority would get nothing outside the Bankruptcy Court, but would get from 50% to 100% under the plan.

The Bankruptcy Court has determined to utilize the "cram down" provision — § 461(11) — to force Petitioners to take less than the amount owed them by Respondent in satisfaction of the debt. The Court has decided that the value of the real property is the value of Petitioners' debt and proposes to hold a hearing to determine that value. Upon payment of the amount determined, Petitioners' security will be taken and their debt discharged.

Petitioners assert that the plan is not feasible, because Respondent cannot realize enough, by sale or refinancing its single asset, to carry out the provisions of the plan. Petitioners assert that it is not in the interest of the creditors, because Petitioners' debt is more than 90% of the total and it would be inequitable and a denial of equal protection to allow a small minority to impose a confiscatory scheme upon Petitioners. Petitioners further contend that the use of the cram down would be an unconstitutional taking of their property without just compensation and would convert the probability of loss by erosion into a certainty.

Petitioners have rights in real property, which is almost universally regarded as being unique. Petitioners assert

that they have the right either to have their loan paid off in full or to have the property. That is the essence of a mortgage. *Radford, supra.* Appraisal may not be utilized as a device to divert value to junior creditors. *Preble v. Wentworth,* 84 F. 2d. 73 (1st Cir. 1936), *cert. den.* 299 U.S. 575, 57 S. Ct. 39, 81 L. Ed. 424 (1936).

The Fifth Amendment prohibits a taking without just compensation. Where the United States has taken property without bargaining or instituting condemnation proceedings, the Tucker Act has been regarded as providing adequate safeguards for the collection of just compensation. This Court has held the Tucker Act available in reorganization cases. *Regional Rail Reorganization Cases,* 419 U.S. 102, 95 S. Ct. 335, 42 L. Ed. 2d. 320 (1974). Between the automatic stay and the cram down, Petitioners will suffer the same erosion and conveyance takings recognized by this Court in the *Rail Cases.*

REASONS FOR GRANTING THE WRIT

I. ONLY THIS COURT CAN ANSWER THE QUESTION WHETHER THE RULES OF BANKRUPTCY PROCEDURE PROMULGATED BY THIS COURT MAY EFFECT AN UNCONSTITUTIONAL TAKING OF A SECURED CREDITOR'S PROPERTY. BECAUSE OF THE EXTRAORDINARY IMPORTANCE OF THE ANSWER TO THE CREDIT MARKETS OF THE NATION, IT IS SINGULARLY APPROPRIATE THAT THIS COURT GRANT EXTRAORDINARY RELIEF.

It has long been established that, in exceptional cases, this court may, in its discretion, grant the relief sought herein. *Ex Parte Republic of Peru,* 318 U.S. 578, 63 S. Ct. 793, 87 L. Ed. 1014 (1943); *Roche v. Evaporated Milk Association,* 319 U.S. 21, 63 S. Ct. 938, 87 L. Ed. 1185 (1943).

It is peculiarly appropriate in this case that the court exercise that discretion because:

(a) There is no adequate remedy by appeal;

(b) This case involves questions of extraordinary importance to the economy of this country; and

(c) This case involves the validity of Rules promulgated by this court.

As explained below, the Chapter XII rules substantially alter the nature of Chapter XII, making it more accessible and, therefore, more subject to abuse.

Moreover, Rule 12-43(a), granting an automatic stay of any action to enforce a lien upon the filing of a petition is, in reality, a delegation of the judicial powers of the United States to the private hands of debtors and bankruptcy lawyers.

There is no requirement in Chapter XII that the petition be judicially scrutinized to determine whether it has been filed in good faith (Cf. § 141, Ch. X, 11 U.S.C. § 541) nor, since the Act was amended in 1952, must the presumed object — an arrangement of debts — be fair and equitable.

The potential for abuse is manifest. In actual practice, that potential is being ever more fully realized.[1]

Increasing publicity[2], together with the demonstrated indifference of the bankruptcy bench to the protection of

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[1]Judge Norton's Opinion (Appendix K), page 7, in footnote 12, points out the increasing frequency of Chapter XII filings. Thus, in the Northern District of Georgia, Chapter XII petitions were filed at the rate of one every 26 *years* from 1938 to Spring, 1974, and one every 24½ *days* thereafter through June, 1976.

[2]E.g., "Chapter XII Bankruptcy: A Grim Case in Atlanta," *Business Week,* November 3, 1975, pp. 70-71.

More recently,

"ATLANTA — Nearly 40 years ago, during the depression, Congress hurriedly passed a hybrid relief bill for some financially

strapped Chicago homeowners who were about to have their mortgages foreclosed.

"The bill became Chapter 12 of the federal Bankruptcy Act, and it worked as intended. But its use was brief, and Chapter 12 sank into obscurity. As recently as three years ago, legal scholars disdained discussing Chapter 12 because its use was so insignificant.

"Now, all that is changing. In the 12 months ended June 30, there were 525 Chapter 12 filings in the U.S., up 88% from 280 the year before and 172 the year before that.

"The resurgence comes at a time when real estate is again in the doldrums. This time, however, it isn't homeowners who are using Chapter 12, because they generally find the Chapter 13 wage-earner's bankruptcy plan to be quicker and cheaper. Instead, it is being used by some relatively sophisticated developers of housing and commercial real-estate ventures.

"Although Chapter 12 was tailored for homeowners in financial difficulty, it also fits many big operators because it applies to individuals or partnerships engaged in ventures with debts secured by property and improvements on it.

Use by Partnerships

"Many big real-estate developments of recent years have been partnerships because of inherent tax advantages to high-bracket developers, and many have debts secured by the real estate involved.

"So while most parts of the bankruptcy act are still used in their traditional roles (Chapters 1 to 7 are for personal failures, Chapter 8 for farmers in trouble, Chapter 9 for municipalities, Chapter 10 for companies in deep trouble, Chapter 11 for those with less serious woes and Chapter 13 for wage earners overburdened by bills), Chapter 12 is coming into unprecedented use. A 1930s set of ground rules is fitting a 1970s situation.

"Bankruptcy experts say the increase is likely to continue because millions of dollars are involved in real estate investment partnerships caught in financial binds. The upsurge in use of Chapter 12 is 'one of the most significant things happening' in federal bankruptcy courts today, according to Kent Presson, assistant chief of the bankruptcy division of the administrative office of U.S. courts."

"Real-Estate Slump Helps to Revive Use of Long-Dormant Bankruptcy Provision." *The Wall Street Journal,* September 29, 1976, p. 40.

secured creditors[3] once the concept of "rehabilitation" — however improbable it may be[4] — has been invoked, has caused massive damage to the credit markets, together with substantial loss of faith and confidence in the ability of the judicial system.[5]

[3]"[U]ntil very recently in bankruptcy history, it has been an open secret that the bankruptcy bar, commercial collection lawyers, referees in bankruptcy and many bankruptcy judges have been openly or covertly hostile to secured creditors. Whether this hostility stems from the traditional reluctance of the law to recognize security interests in property of a debtor which he retains and uses from the position accorded by existing law to the secured creditor in bankruptcy and other insolvency proceedings, from the Shylock image given to all lenders of money or from the self-interest of the hostile groups in having available the largest possible pot for fees and allowances to themselves, it is difficult if not impossible to discern. . . . That lawyers, and particularly judges, could and should do so without regard to the impact of their handiwork on the availability and costs of credit, to the business community, in particular, is almost incomprehensible." Paul R. Moo, "The Secured Creditor in Bankruptcy," 47 *American Bankruptcy Journal 23,* 23-4 (1973).

[4]Few Chapter XII cases result in published decisions. See, however, *Rader* v. *Boyd, Sumida* v. *Yumen,* cited *infra* in point II.

[5]This is nothing new. More than forty years ago, the Senate investigated Bankruptcy and Receivership proceedings. Shocked by what they found, the committee reported: "[H]owever much the course of action of the courts in handling receiverships has fallen below our conception of the accepted standards of jurisprudence, it is yet less reprehensible than has been that conduct of a bankruptcy proceeding brought to our notice in the course of our investigation, and to which reference is made elsewhere in this report.

"As we review in perspective the tortuous course of that proceeding, we are led to pause and to wonder how long a system of laws, so administered, can endure or continue to have or to merit the confidence of the people." Senate Rpt. Preliminary Report, Special Committee on Investigations of Bankruptcy and Receivership Proceedings in United States Courts, 73rd Cong. 2nd Session, Report No. 364 (February 20, 1934), hereinafter referred to as "Senate Investigation."

Secured creditors — their hands tied by injunction; their security deteriorating, both physically and by the continuing accruals of prior encumbrances, such as taxes; their funds tied up involuntarily (with no return on their investment[6] and no opportunity to make alternate use of their funds) — have a limited number of options:

(a) fight, hoping they won't be hurt too badly. (The "Home Court Advantage" in bankruptcy favors the debtor);

(b) quit[7];

(c) finance the proceedings, hoping they won't be hurt too badly; or

(d) submit to extortive demands.[8]

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[6]Consider the secured Real Estate Investment Trust. In order to operate as an REIT, at least 90% of earnings must be distributed annually to shareholders. As a practical matter, many REITs distribute 100%. Thus, dollars tied up in futile attempts to rehabilitate speculative ventures are directly lost by thousands of individuals, pension funds, etc. nationwide.

[7]Consider the subordinate lienholders. Over the course of the Chapter proceeding — which may be measured in terms of years — the amount of prior encumbrances might increase so much that the lienholder cannot afford to maintain his position. Whatever value his equity position might have had at the outset of the proceedings, then, has been destroyed.

[8]E.g., in *In re Beverly Hills Bancorp,* USDC, Central District of California No. BIC 74-4409, a $15,000,000 first lienholder on an uncompleted project, in which the debtor had nothing more than a subordinate interest, had to pay $825,000 to the Trustee in order to gain leave to foreclose.

And, in a Chapter XI case, *In re W. T. Grant Co.,* USDC, SDNY, Bankruptcy No. 75 B 1735 W. T. Grant landlords were compelled to surrender all claims — and, in some instances, pay money to the estate— in order to recover their own property.

To state the case simply: Chapter XII has become a license to speculate with others' money. And if it can be used as threatened by Bankruptcy Judge Norton[9], it becomes a license to steal.

Clearly, appeal is no remedy in this situation. The loss is continuous and, except as to the possible liability of the United States,[10] there is no recourse. Moreover, this matter involves the validity of Rules promulgated by this court and it is *this* court which must make the ultimate decision as to whether they are in conflict with the Constitution and whether they are in conflict with the policy of Congress as embodied in the Bankruptcy Act, so as to exceed Congress' ability to delegate legislative powers.

In *U.S. Alkali Export Assn. v. U.S.,* 325 U.S. 196, 65 S. Ct. 1120, 89 L. Ed. 1554 (1945), this court issued common law certiorari because:

> "The hardship imposed on petitioners by a long postponed appellate review, coupled with the attendant infringement of the asserted Congressional policy of conferring primary jurisdiction on the Commission, together support the appeal to the discretion of this Court to exercise its power to review the ruling of the district court in advance of final judgment." 325 U.S. at 204.

And, in *DeBeers Consol. Mines v. U.S.,* 325 U.S. 212, 65 S. Ct. 1130, 89 L. Ed. 1566 (1945), the situation justifying the writ was the fact that a decision on the merits could not redress the injury done by the injunction. Unless it could be reviewed by extraordinary writ, there would be no remedy.

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[9]Opinion, Appendix K.

[10]*Infra,* Point V.

The analogy to the Rule 12-43(a) situation is persuasive. It is interesting to note the further parallels with *DeBeers:* the restraining order was there obtained without notice or opportunity to be heard (as here) and the injunction would have been unobtainable under state law (as here).

Los Angeles Brush Mfg. Corp. v. James, 272 U.S. 701, 47 S. Ct. 286, 71 L. Ed. 481 (1927), involved the Equity Rules, which gave the petitioner the right to trial in open court. The District Court judges in the Southern District of California, however, had agreed to refer all patent cases to a master. Other than the writ sought in this court, the petitioners would have had no other remedy for the violation of their right to trial.

This Court pointed out that normally, the matter would go through the Ninth Circuit, but

> ". . . we think it clear that where the subject concerns the enforcement of the Equity Rules which by law it is the duty of this Court to formulate and put in force, and in a case in which this Court has the ultimate discretion to review the case on its merits, it may use its power of mandamus and deal directly with the District Court in requiring it to conform to them. *Ex Parte Abdu,* 247 U.S. 27, 28; *Ex Parte Crane,* 5 Peters 190, 192, 193, 194 . . . The question of thus using the writ of mandamus would be a matter of discretion in this Court . . ."[11] 272 U.S. at 706.

See also *LaBuy v. Howes Leather Co.,* 352 U.S. 249, 77 S. Ct. 309, 1 L. Ed. 2d. 290 (1957), reh. den. 352 U.S. 1019, 77 S. Ct. 553, 1 L. Ed. 2d. 560 (1957), where this

[11]Having expressed its opinion, the court was confident that it need not actually issue the writ. Apparently, it was wrong. *McCullough v. Cosgrave,* 309 U.S. 634, 60 S. Ct. 703, 84 L. Ed. 992 (1940) was a per curiam opinion directed to the same district court vacating the reference of two patent cases to a master.

court granted certiorari because of the importance of the question in administration of the FRCP and *Schlagenhauf v. Holder,* 379 U.S. 104, 85 S. Ct. 234, 13 L. Ed. 2d. 152 (1964), where this court granted certiorari to review undecided questions concerning the validity and construction of FRCP 35.

II. THIS COURT HAS NO CONSTITUTIONAL POWER TO LEGISLATE AND CONGRESS CANNOT CONSTITUTIONALLY DELEGATE TO IT THE POWER TO REPEAL ACTS OF CONGRESS.

Title 28 U.S.C., § 2075, provides, in relevant part:

> "The Supreme Court shall have the power to prescribe by general rules the forms of process, writs, pleadings and motions, and the practice and procedure under the Bankruptcy Act.
>
> "Such rules shall not abridge, enlarge or modify any substantive right . . . .
>
> "All laws in conflict with such rules shall be of no further force or effect after such rules have taken effect."

Pursuant to this authority, this Court promulgated rules under Chapter XII, which became effective August 1, 1975. By the terms of the statute, rules which conflict with those Bankruptcy Laws previously enacted by Congress and in effect as of the effective date of the rules repeal those Acts of Congress.

In view of the clear delineation of powers contained in the Constitution,[12] it becomes necessary to inquire, first, as to the extent to which Congress may delegate its legislative powers; second, whether the purported delegation was with-

[12]Article 1, § 1: "All legislative powers herein granted shall be vested in a Congress of the United States . . . ."

Article III, § 1: "The judicial power of the United States shall be vested in one Supreme Court, and in such inferior courts as the Congress may from time to time ordain and establish."

in the permissible limits; and third, whether Congress did, or could, *delegate* the power to adopt the Chapter XII rules that became effective August 1, 1975.

The enabling statute calls for the prescription of rules which "shall not abridge, enlarge or modify any substantive right." In order to determine whether the Rules satisfy this limitation, it is necessary to examine the law as legislated by Congress compared to the laws as legislated under Congress' delegation.

Preliminarily, it must be observed that this situation is unlike others wherein this Court has promulgated rules, for the reason that the Bankruptcy Act itself is primarily a procedural law, containing explicit provisions governing bankruptcy proceedings.[13]

Proceedings in Chapter XII are commenced by the debtor's filing a petition.[14] The Act defines a petition as "a petition filed under this chapter *proposing an arrangement* by a debtor."[15] (Emphasis added) It must "state that the debtor is insolvent or unable to pay his debts as they mature, and *shall set forth the terms of the arrangement proposed by him*."[16] (Emphasis added)

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[13]See, in addition to the Act, the Advisory Committee's Introductory Note to the Preliminary Draft:

"Because it has not been necessary heretofore in the drafting of bankruptcy legislation to distinguish between substantive and procedural provisions, they are interwoven throughout the Act." 1976 Collier Pamphlet Edition, *Bankruptcy Act and Rules,* Part 2, Bankruptcy Rules, p. 751 (1976).

[14]11 U.S.C. § 821-2.

[15]11 U.S.C. § 806(9).

[16]11 U.S.C. § 823.

After a petition has been filed, the court "shall promptly call a meeting of creditors, upon at least 10 days' notice. . . ,"[17] which "shall be accompanied by a copy of the proposed arrangement . . ."[18] At that meeting the court shall examine the debtor, may allow or disallow proofs of claim and shall receive and determine the written acceptances of creditors on a proposed arrangement.[19] Upon acceptance, the court shall fix times for deposit of the monies to be distributed and for the application for and hearing on confirmation of the arrangement.[20]

The leading commentator points out that these statutory provisions of Chapter XII "serve to expedite the administration of the proceeding." 9 *Collier on Bankruptcy* 14th Edition ¶ 5.04, p. 919-20.

Clearly, Chapter XII, as conceived by Congress, was to provide an expedited procedure,[21] compared to other chapters of the Bankruptcy Act, whereby a debtor who qualified for Chapter XII could propose an arrangement with his creditors and have that arrangement either accepted and confirmed or rejected. This has been recognized by the courts (e.g. *Sumida v. Yumen,* 409 F.2d 654, 660 (9th Cir. 1959), *cert. den.* 405 U.S. 964, aff'd 444 F.2d 1281: "Thus, adherence to the normal procedure in Chapter XII cases should not produce any inordinate delay.")

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[17]11 U.S.C. § 834.

[18]11 U.S.C. § 835.

[19]11 U.S.C. § 836.

[20]11 U.S.C. § 837. See also 9 Collier on Bankruptcy, ¶ 5.04.

[21]See 9 Collier on Bankruptcy, ¶ 4.06[5], footnote 15:

" 'The filing of a plan as a part of the original petition should avoid much delay. In the absence of such provision, as in present Section 74, the debtor is often enabled to delay the presentation of his proposals for an unreasonably long period.' Analysis of H.R. 12889, 74th Cong., 2nd Sess. (1936) 100 H.R. 12889 is the forerunner of the Chandler Act."

The Rules completely alter the workings of Chapter XII. Rule 12-36 dispenses with the requirement that the plan be filed with the petition[22] and the requirement that the plan be transmitted along with the notice of the meeting of creditors[23] (which need no longer be called promptly, but must be held between 20 and 40 days after the filing of the petition, subject to further delays due to various motions and appeals).[24]

The application or motion, determination of which may further delay the meeting of creditors, may initially only be made by the debtor.[25]

From this single example, it can be seen that the Rules change the entire character of Chapter XII. As pointed out by Bankruptcy Judge Norton,[26]

> "Prior to 1975, perhaps a deterrent to the use of Chapter XII was contained in the provisions then applicable, which required a plan of arrangement to accompany the petition upon filing, and that a trustee be appointed immediately. Naturally, the additional costs and loss of control resulting from a trustee is abhorrent to a debtor who desires continued possession and control of the business. However, the recently enacted Bankruptcy Rules, enacted effective August 1975, change both of these requirements. Bankruptcy Rule 12-17 contemplates continued possession by the debtor unless there is some reason for appointment of a trustee. If no trustee is appointed, § 444 provides that the debtor continues in

[22]Rule 12-36(a).

[23]Rule 12-36(d).

[24]Rule 12-24(a)(1).

[25]Rule 12-41.

[26]Appendix K, p. 16 (footnote 32).

> possession of his property and in such status is a trustee for all practical purposes. See Rule 12-17 and *In re Walker*, 93 F.2d 281 (2d Cir. 1937). Also, Bankruptcy Rule 12-36 offers the debtor more flexibility now than the restrictive §§ 423 and 534 by providing that the plan may be filed with the petition "or thereafter" at a time as approved by the court. And, § 466 allows a creditor or creditors under certain conditions to file a plan."

As Judge Norton points out, the other *major* change wrought by the Chapter XII Rules is one which allows the debtor to retain *(or regain)* control over the property. Section 432 of the Act (11 U.S.C. § 832) allows the Court to appoint a trustee upon the application of any party in interest. Rule 12-17(b), by contrast, requires the applicant to show cause — a difficult task, in the bankruptcy court. Moreover, if the secured creditor has acted to protect his security by obtaining the appointment of a receiver in the state court, Section 507 (11 U.S.C. § 907), together with Rule 12-17, requires the receiver to return the property to the debtor. Again, this drastic infringement upon the creditor's property rights is automatic upon the mere filing of a Chapter XII petition.

If it is true, as bankruptcy lawyers and judges are fond of observing, that:

> " 'Everyone who takes a mortgage or a deed of trust intended as a mortgage, takes it subject to the contingency that proceedings in bankruptcy against his mortgagor may deprive him of the specific remedy which is provided for in his contract.' *In re Jersey Island Packing Company*, 138 F. 625, 627 (9th Cir. 1905),"

then it must be true that Petitioners' security deeds were executed, in 1973, in contemplation of the Bankruptcy law enacted by Congress — i.e., the Bankruptcy Act. If it is

true, as Bankruptcy Judge Norton observes — and the statistics cited by him[27] seem to indicate that it is — that in 1973, Chapter XII proceedings were difficult and undesirable for debtors to commence, then it must have been contemplated that there was virtually no risk that Petitioners would become ensnared in a Chapter XII proceeding. After all, there had only been one in the Atlanta area in 25 years! If it is true, as this Court stated in *Louisville Joint Stock Land Bank v. Radford,* 295 U.S. 555, 55 S. Ct. 854, 79 L. Ed. 1593 (1935), that legislation cannot deprive petitioners of rights in the specific property securing their loans, especially when those rights were secured prior to the legislation, then it is evident that the Chapter XII Rules, effective August 1, 1975, cannot constitutionally be applied to take petitioners' property.

Thus, it is evident that the Rules have wrought substantive changes in the nature of Chapter XII exceeding the bounds of 28 U.S.C. § 2075 and, *a fortiori,* they exceed the limits of delegable legislative power.

Prior to the enactment of 28 U.S.C. § 2075, Section 30 of the Bankruptcy Act invested this Court with the authority to prescribe all necessary rules, forms and orders as to bankruptcy procedure. Pursuant to the authority conferred by Section 30, this Court promulgated numerous General Orders and Forms, which it soon became necessary to reconsider. In *Meek v. Centre County Banking Co.,* 268 U.S. 426, 45 S. Ct. 560, 69 L. Ed. 1028 (1924), for example, a petition had been filed in accordance with General Order in Bankruptcy No. 8 and Bankruptcy Form 2, which allowed one or less than all partners to file a petition against the partnership without the consent of the remaining partners. By contrast, the Act provided only two methods for the commencement of a partnership bank-

[27]Appendix K, p. 5 (footnote 12).

ruptcy proceeding: by voluntary petition (contrasted to the situation before the Court where the other partners resisted) and by involuntary petition filed by the partnership's creditors.[28]

Comparing the two, this Court correctly concluded that General Order No. 8 and Form No. 2

> "do not relate to the execution of any of the provisions of the Act itself; and therefore are without statutory warrant and of no effect." 268 U.S. 426, 434.

The point of the *Meek* case is that authority to make rules "is plainly limited to provisions for the execution of the Act itself, and does not authorize additions to its substantive provisions."[29] This point had long since been declared in *West Co. v. Lea,* 174 U.S. 590, 19 S. Ct. 836, 43 L. Ed. 1098 (1899), an early case where the rules which had been promulgated by this court provided for an issue as to solvency in involuntary bankruptcy cases, whereas the Act made that issue irrelevant. In holding that a plea of "not insolvent" was no defense, this Court observed:

> "These rules were but intended to execute the act, and not to add to its provisions by making that which the statute treats in some cases as immaterial a material fact in every case." 174 U.S. 590, 599.

This and other courts have had numerous occasions to pass upon the validity of Rules promulgated by this Court. See, for example, *Damon v. Damon* 283 F.2d 571 (1st Cir. 1960) (General Order 30); *Los Angeles Brush Mfg. Co. v. James, supra; McCullough v. Cosgrove, supra)* (Equity Rules); *LaBuy v. Howes Leather Co., supra* (FRCP);

[28]Note the primarily procedural aspects to the pertinent parts of the Act and the General Order and Form.

[29]268 U.S. 426, 434.

Schlagenhauf v. Holder, supra and *Sibbach v. Wilson* Co., Inc., 312 U.S. 1, 61 S. Ct. 422, 85 L. Ed. 479 (1941) (FRCP 35(a)), and *In Re State Thread Co.,* 126 F.2d 296 (6th Cir. 1942).[30]

The need for this Court to determine the validity of its own rules is amply demonstrated by the recent District Court cases of *In Re Garcia* (C.D. Cal. 1975) 396 F. Supp. 578, holding Rule 13-307(d) valid; *Wolff v. Wells Fargo Bank* (N.D. Cal. 1975), 400 F. Supp. 1352, holding the same Rule invalid. In *In Re Wall,* (E.D. Arkansas 1975), 403 F. Supp. 357, the court, reviewing the two California cases, as well as pre-rule authorities, found a split of authority in the "few cases . . . which even discuss the issue." This Court, the District Judge pointed out, has had no occasion to settle the differing results between and within the circuits. In concluding the Rule to be valid, the Court utilized "a strong presumption that the Supreme Court did not abridge or modify any substantive right by the rules."[31] Had this Court overstepped the authority delegated by Congress, the Court presumed "such transgressions would have been noted and the offending rule modified or deleted upon review."[32]

Only this Court can determine whether the *Wall* Court was correct. Mr. Justice Douglas, dissenting from this Court's Orders prescribing the Bankruptcy Rules and

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[30]This case illustrates the difficulty, even for members of this Court, in agreeing whether a rule is procedural or substantive. See also *U.S. v. Sherwood,* where this Court found that the Court of Appeals (2d Cir.) had confused procedure with jurisdiction. 312 U.S. 584, 589, 61 S. Ct. 767, 85 L. Ed 1058 (1941).

[31]403 F. Supp. 357, 360.

[32]*Id.*

Official Bankruptcy Forms, and, later, Chapter X Rules, said:

> "The Court is merely the conduit for the Rules. It does not purport to approve or disapprove. As I have said on other occasions, it has merely placed its imprimatur on the Rules without reading, let alone discussing, these Rules." 411 US 992, 37 L. Ed. 2d xxxi (1973).
>
> "As I have said before, 'I cannot agree to the Court's submission of the proposed Bankruptcy Rules to the Congress' . . . Because this Court is no more than a 'rubber stamp', I think it should not participate in the rule-making process." 421 US 1021, 44 L. Ed 2d xxxiii (1975).

It may be that the changes made in Chapter XII by the Rules are changes which Congress might find desirable.[33] The wisdom of taking such action, of course, is a matter of policy, which should remain the concern of Congress. *Home Bldg. & Loan Ass'n v. Blaisdell,* 290 U.S. 398, 54 S. Ct. 231, 78 L. Ed. 413 (1934).

Even if the changes wrought in Chapter XII by the Rules were determined to be merely procedural, however, that would not end the question. As pointed out, a large proportion of the Act itself is procedural. To the extent that a Rule contradicts a portion of the Act, then, that Rule is repealing an Act of Congress.

It is no answer that 28 U.S.C. § 2075 gives this Court the power to do so. *Marbury v. Madison,* 1 Cranch [5 U.S.] 137, 2 L. Ed. 60 (1803).

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[33]Several years ago, Section 323 of the Act (11 U.S.C. § 723) was amended to relieve the Chapter XI debtor from the obligation of accompanying his petition with a plan of arrangement — the same change effected, in the case of the Chapter XII petition, by Rule

Congress cannot abdicate or transfer to others the essential legislative functions vested in it by the Constitution. *Panama Refining Co. v. Ryan,* 293 U.S. 388, 55 S. Ct. 241, 79 L. Ed. 446 (1935); *Schecter Corp. v. United States,* 295 U.S. 495, 55 S. Ct. 837, 79 L. Ed. 1570 (1935).

As this Court pointed out therein, in every case prior to *Panama* in which the question had been raised, the Court had recognized that there are limits of delegation which there is no constitutional authority to transcend.[34]

This is not to say that Congress is to be denied that flexibility that a limited delegation would provide. The essen-

12-36. The legislative change was apparently no more than a recognition of the fact that bankruptcy judges were often ignoring the law in order to help debtors into the protective arms of the bankruptcy courts.

Prior to enactment of that legislation, Mr. W. Randolph Montgomery, for the National Bankruptcy Conference, had, on May 21, 1958, told a Subcommittee of the Committee on the Judiciary, United States Senate:

> ". . . In view of the fact that the act makes the filing of a copy of arrangement with the petition mandatory, lip service has been given to that requirement where the requirement has been met at all. So-called plans of arrangement accompany petitions in those cases which the debtor himself has no serious expectation of ever consummating. In other instances the courts, having found that it is not practical to have a definitive plan of arrangement accompany the petition, have closed their eyes and ears to the mandatory requirement of the statute that the arrangement accompany the petition and have allowed a time for the filing of a plan of arrangement.
>
> "Of course, that is entirely extralegal and there is no authority for it in the act."

Senate Report No. 118, *U.S. Code, Cong. & Admin. News,* 85th Cong. 2d Sess. 1958.

Chapter XII has no creditors' committee analogous to the Chapter XI committee. See Act, § 339 (11 U.S.C. § 739).

[34]293 U.S. 388, 430.

tial question appears to be whether the delegatee is constrained to follow the standards established by Congress, or whether there is a broader, less fettered discretion. *Schecter, supra; Panama, supra.*

> ". . . The Congress . . . may establish primary standards, devolving upon others the duty to carry out the declared legislative policy, that is, as Chief Justice Marshall expressed it, 'to fill up the details' under the general provisions made by the legislature. *Wayman v. Southard,* 10 Wheat. 7, 43." 293 U.S. 388, 426.

The concept behind the Congressional policy — as manifested by the statutory provisions of Chapter XII — is incompatible with the concept behind the Rules ostensibly enacted to execute that Congressional policy. One policy must prevail and it must be that of Congress.

From the above, it is apparent that this Court cannot be authorized by Congress to enact Rules which repeal enactments of that Body without first amending the Constitution.

It was not without reason that this came to be. This country was founded in rebellion against the tyranny of English colonial government. To preserve their newly won freedom, the founding fathers deliberately framed a Constitution that would limit the powers of the federal government, and provided "checks and balances" within the government as to its exercise of those powers given. The functions of the three branches were clearly and separately delineated.[35] The Constitution was declared to be the

[35]Article I, Section 1: "All legislative Powers herein granted shall be vested in a Congress of the United States . . ."

Article II, Section 1: "The executive Power shall be vested in a President of the United States of America . . ."

Article III, Section 1: "The judicial Powers of the United States shall be vested in one Supreme Court, and in such inferior courts as the Congress may from time to time ordain and establish."

supreme law of the land[36] and was insulated from being changed by the federal government.[37] The Bill of Rights was added.

The result was a government of laws — not of men.[38]

It is that Constitution that dictates the powers and functions of this Court and of Congress. Congress cannot, in contravention of those dictates, either create new powers in this Court (*Marbury v. Madison, supra*) or abandon to this Court its own powers. Thus, a legislative act of Congress may be declared unconstitutional by this Court (*Marbury v. Madison, supra*), but it cannot be *repealed* by this Court.

[36]Article VI.

[37]Article V.

[38]See the discussion by Dean Roscoe Pound in *The Development of Constitutional Guarantees of Liberty,* Yale University Press, New Haven and London (1963).

> "Teachers have been telling us that the separation of powers was only a fashion of eighteenth-century political thought, derived from a forecast made by Aristotle, for there was nothing of the sort in his time, and a mistaken interpretation of the British policy of his time by Montesquieu. We are told that it is outmoded and ought to give way to the exigencies of efficient administration. Recently this has spread to at least one of the courts which intimates that this fundamental principle of our constitutions should not be taken too seriously under the conditions of the time. Nothing could be more mistaken. When in the controversies which led to the Declaration of Independence, hostility to things English led to finding a philosophical basis for the rights which lawyers had learned as the rights of Englishmen, natural rights were put as the ground of what the English had learned from experience. The separation of powers was no more derived from political philosophy than the rights secured by the Bill of Rights. It was taken up as the result of experience and reinforced by reference to Montesquieu. Whether put as common-law rights, the liberties claimed by generations of Englishmen and insisted on by the colonists as their birthright were seen to be incompatible with unlimited centralized power." (Page 95)

To the extent that the Rules repeal the Acts of Congress, then, they are invalid, being beyond the power of the Court to enact — even with the purported blessing of Congress — because authorization cannot be made by Congress.

If Congress wishes to make radical changes in Chapter XII, *Congress* must do so.

III. THE CHAPTER XII RULES ARE UNCONSTITUTIONAL BECAUSE THEY DEPRIVE SECURED CREDITORS OF THEIR PROPERTY WITHOUT NOTICE OR OPPORTUNITY TO BE HEARD AND WITHOUT ADEQUATE SAFEGUARDS TO PROTECT AGAINST A CONTINUOUS TAKING OF THE SECURED CREDITOR'S PROPERTY WITHOUT JUST COMPENSATION.

A. THE AUTOMATIC STAY DEPRIVES SECURED CREDITORS OF PROPERTY WITHOUT NOTICE OR OPPORTUNITY TO BE HEARD.

Rule 12-43(a) provides:

> "(a) Stay of Actions and Lien Enforcement. A petition filed under Rule 12-6 or 12-7 shall operate as a stay of the commencement or the continuation of any court or other proceeding against the debtor, or the enforcement of any judgment against him, or of any act or the commencement or continuation of any court proceeding to enforce any lien against his property, or of any court proceeding for the purpose of the rehabilitation of the debtor or the liquidation of his estate."

This matter is distressingly typical of Chapter XII proceedings.[39] An over-leveraged, undercapitalized debtor, on

[39]See footnote k, *supra,* and Appendix L.

the eve of foreclosure of its sole asset, invokes the power of the United States to prevent that foreclosure. No showing of good faith is required or made, no plan is proposed nor, in most cases, is any plan feasible.[40]

The debtor merely asserts that it intends to propose a plan.

The foreclosing creditor — often a pension fund, Real Estate Investment Trust or other publicly-owned entity — *already* has a problem loan on its hands *before* the filing. It may have millions of dollars tied up in the project. It may have already spent months trying to work with the borrower. It may not have received any return on its investment for an extended period. Apart from the return originally expected, usually limited in the case of secured transactions because heretofore they were considered less risky, the creditor may be faced with the prospect of not being able to even recoup its loan.

The creditor must make the best of a bad situation. Perhaps another bidder will be successful, or perhaps the creditor will purchase the property and then find a buyer. In either case, it may be able to limit its loss on *this* loan and put the money to productive use elsewhere. Perhaps the debtor was financially unable to complete the project or to operate it. The creditor, on the other hand, with more resources available, may, on acquisition, choose to complete and/or operate the property in order to enhance its value and increase its chances of losing less.

One principal means of limiting the creditor's loss is to deal with the problem quickly, for time is the worst

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[40](Other than the procedure proposed in this matter to take property from the secured creditors to pay the other creditors.) See point IV, *infra*, p. 60.

enemy. The creditor must ordinarily pay for the money it has loaned to the debtor.[41] The situation would be otherwise, were the debtor able to make payments on the loan from the income of the property, or willing (as in the case of a limited partnership-debtor) to invest some additional capital to save its own investment. Then the passage of time would not be so catastrophic to the creditor.

But the debtor is, by definition, insolvent.[42] By simply filing a petition — *by writing its own injunction,* thanks to § 428 and Rule 12-43(a) — it can *shift the entire risk to the creditor!*

The debtor, facing foreclosure, has nothing to lose. If its "impossible dream" miraculously comes true, it wins. Otherwise, it can walk away no worse for having tried. And perhaps, along the way, the desperate secured creditor might be willing to pay "walk-away" money to be relieved of the injunction.[43]

In any event, after filing by a debtor, the game henceforth will be played with the creditors' money. See, for example, *Rader v. Boyd,* 267 F.2d 911 (10th Cir. 1959), a bitter and protracted proceeding that made its way through the appellate courts at least twice,[44] where the Court, recalling its characterization of the debtor's first proposal as

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[41]Many REITs are currently obligated to pay as much as 130% of the bank's prime lending rate.

[42]Section 423 (11 U.S.C. § 823).

[43]It is widely known that creditors, faced with the prospect of interminable delays, often surrender to the coercive economic pressures imposed upon them by the passage of time and accede to requests that they pay money to a debtor or trustee in order to gain relief from the injunction. See Part I Footnote 8.

[44]See also 252 F.2d 585 (10th Cir. 1958).

"a speculative venture with accrued funds belonging to the secured creditors," went on to observe:

> "The second proposal is a speculative venture with funds obtained by the pledge of the property constituting the security of the creditor Boyd. There is no essential difference. In each instance the security of the creditor Boyd is to be used to finance a venture, the outcome of which is clouded with doubt."

Or, see *Sumida v. Yumen, supra,* cit. p. 654: " '. . . The proceeding was merely an attempt to delay creditors in a situation in which there was no possibility that a Chapter XII proceeding could be successfully completed. . . . We think the debtors are engaging in an exercise of futility and appreciate the trial court's desire to terminate the proceedings.' "

The secured creditor, enjoined from foreclosing by Rule 12-43(a), made to bear the risk of the failure of the debtor to realize his Chapter XII visions, unable to control the property[45] — even if, pursuant to the provisions of the mortgage or trust deed and the applicable state law, it had obtained the appointment of a receiver for the property[46] — must watch the travesty unfold, knowing, all the while, *that it must continue to pay for the money* the debtor's "self-help" injunction has put out of reach.

In *Radford, supra,* this Court enumerated several property rights possessed by the secured creditor "who has rights

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[45]The scheme of Chapter XII is to provide for a "debtor-in-possession." See § 444 (11 U.S.C. § 824). See also 9 Collier on Bankruptcy, ¶ 6.04, p. 981.

[46]The receiver is ousted in favor of the "debtor-in-possession". See § 507 (11 U.S.C. § 907). 9 Collier on Bankruptcy ¶ 6.04, § 12.02.

in specific property," contrasting his position to that "of an unsecured creditor, who has none . . ." 295 U.S. at 588.

The rights enumerated in *Radford,* as provided by the law of Kentucky, were:

> "1. The right to retain the lien until the indebtedness thereby secured is paid.
>
> "2. The right to realize upon the security by a judicial public sale.
>
> "3. The right to determine when such sale shall be held subject only to the discretion of the court.
>
> "4. The right to protect its interest in the property by bidding at such sale whenever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale or by taking the property itself.
>
> "5. The right to control meanwhile the property during the period of default, subject only to the discretion of the court, and to have the rents and profits collected by a receiver for the satisfaction of the debt." 295 U.S. at 594.

A petition, initiating a Chapter XII proceeding as conceived by Judge Norton, immediately threatens the loss of *all* the property rights recognized by this Court in *Radford.*

How does the secured creditor lose the property rights it has bargained for?

Automatically.

Without notice, without any opportunity to be heard.

As pointed out previously, there is no judicial review of the petition prior to filing. The debtor has written his own injunction.

In Georgia, if a foreclosure sale is prevented, it cannot be had until the first Tuesday of the following month, and only then if the Court allows the creditor to *immediately* commence advertising; otherwise, it will be impossible to advertise four consecutive weeks within the same calendar month, and the minimum delay in foreclosure would be two months. Although Rule 12-43(e) provides for *ex parte* relief, it is rarely, if ever, granted.[47]

[47]For example, in a recent case in the same district as the instant matter, a Chapter XII petition was filed on August 2, 1976, the day before the second lienholders' foreclosure sale. The second lienholders (two REITs) filed a complaint seeking leave from the stay and made application under 12-43(e). Their application showed them to be subordinated to a 6.6 million dollar loan. The monthly payments on the loan, together with impounds for real property taxes, amounted to $60,705. The debtor was a tax-shelter limited partnership whose single asset was a medical office building less than 44% leased, with a cumulative deficit for the first seven months of 1976 of $508,909.05 (*excluding* interest on the subordinated loan). Moreover, projected income at 95% occupancy would be insufficient to service the project's debt and the debtor's experience indicated that it would take approximately a year and one-half to reach 95%. By its terms, the subordinated loan of approximately 1.2 million dollars matured on August 30, 1976.

The lienholders sought relief, so they could complete the scheduled sale or, in the alternative, that the stay be conditioned upon the debtor's being required to post security or pay rent to protect the lienholders against the $60,705 needed monthly to prevent default on the first lien.

The Bankruptcy Judge denied relief, despite the apparent abuse. The lienholders sought mandate in the District Court, which issued an Order to Show Cause. Several days later, the District Court, while expressing grave doubts as to the constitutionality of the automatic stay, vacated his Order to Show Cause on the ground that mandate was not the appropriate remedy. (*B & B Properties, Ltd,* Northern District of Georgia, Atlanta Division, B76-2377A.)

Assume a 1.5 million dollar loan, with lender's cost of funds at 8 percent. The mere filing of a Chapter XII petition in Georgia, even if the lienholder is allowed immediately to commence advertising the sale, will result in a minimum one month delay. This is, in effect, an involuntary one-month interest-free loan. And the loss of that month will cost the lender $10,000 *out of pocket*.

The longer this situation continues, the worse it becomes — the amount of the lender's loss is a function of time. In addition, the lender may be forced to make other payments, such as Petitioners herein did.[48]

None of the most blatant abuses of Chapter XII could be accomplished without the injunction and the Bankruptcy Court has no discretion to refuse it; thus the *key* to the debtor's capacity to do harm is the automatic feature of the 12-43(a)/§ 428 stay, issued with no judicial scrutiny, no notice, no opportunity to be heard, no form of protection (such as would be required in the state court — see *Georgia Code Annotated,* § 81A-165C, or the District Court — see FRCP, § 65(1)) is afforded, and there is no way to recover damages, the debtor being insolvent.

This is what happens when a petition is filed. It is true no matter whether the debtor has other assets or funds to contribute, giving it a reasonable chance to make a plan feasible, or where it is merely a cynical abuse of the judicial process. The availability of the automatic stay, coupled with the relative indifference of the bankruptcy courts to

[48]According to testimony presented in the Bankruptcy Court on April 1, 1976, Petitioners paid $15,554.98 of their own funds on December 16, 1975, to pay the debtor's property tax obligations. Almost a full year has since expired and taxes must again be paid. Who should have to pay them?

the secured creditors' rights,[49] results, inevitably, in the wasteful taking of property from lenders for no reason

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[49]Professor Moo observes, "At least until very recently in bankruptcy history, it has been an open secret that the bankruptcy bar, commercial collection lawyers, referees in bankruptcy and many bankruptcy judges have been openly or covertly hostile to secured creditors." Moo, *The Secured Creditor in Bankruptcy, supra,* p. 23.

Compare the views of Professor Vern Countryman, former Vice President of the National Bankruptcy Conference, who characterizes the secured creditor as a "grabber," who will selfishly insist on his rights, even though the result may be "that nothing is left even for the payment of expenses of administration." "Hence it is that I have sought to devise some arguments that may be used to *reduce the size of the grab* in bankruptcy proceedings. . . . If these arguments, or others, do not succeed, there is another alternative. The Bankruptcy Act can be amended. . ." [Emphasis added] Countryman, *Code Security Interests in Bankruptcy,* 75 Commercial Law Journal, p. 269 (1970).

(It appears that *another* alternative has already been found — cancel the Act with new Rules.)

Professor Moo, noting Professor Countryman's concern that the fees and expenses of bankruptcy be paid, and asserting his faith that the draftsmen of the Uniform Commercial Code were aware of Article VI § 2 of the Constitution, states:

> "The issue is whether or not the Bankruptcy Act is to be misused as a vehicle for interfering with or prohibiting, in an economic sense, the creation of security interests by the consumer, farmer or businessman who wishes to use his property to obtain credit or to obtain his credit requirements at a lower cost by collateralizing his obligations. To the extent that the Bankruptcy Act is construed or amended to subordinate or invalidate security interests permitted by state or other federal laws, it becomes an instrument of social or governmental policy dictating how and in what respect or subject to what burdens, the consumer, farmer or businessman may use his assets to conduct his own affairs. Constitutional issues aside, the real question is the extent to which Congress, under its bankruptcy or other powers, should interfere with or burden or regulate the debtor's use of his own property to obtain credit or his use of secured credit in obtaining other property."

other than the ritual invocation of the "rehabilitation" of the debtor. It is very easy, having filed a petition for a debtor, to claim to be in the process of rehabilitation, but saying so does not make it true — and it seldom is true. While some may hold that man can accomplish whatever man can conceive, the record shows an abysmally low correlation between petitions and rehabilitations.

Does this conflict with the Constitutional guarantee of Due Process?

It does if the principles recently enunciated by this Court are still viable. See *Sniadach v. Family Finance Corp. of Bay View,* 395 U.S. 337, 89 S. Ct. 1820, 23 L. Ed. 349 (1969); *Fuentes v. Shevin,* 407 U.S. 67, 92 S. Ct. 1983, 32 L. Ed. 2d. 556 (1972) *reh den* 409 U.S. 902, 93 S. Ct. 177, 34 L. Ed. 2d. 165 (1972); *Goldberg v. Kelley,* 397 U.S. 244, 90 S. Ct. 1011, 25 L. Ed. 2d. 287 (1970); *North Georgia Finishing, Inc. v. Di-Chem, Inc.,* 419 U.S. 601, 95 S. Ct. 719, 42 L. Ed. 2d. 751 (1974); *Mitchell v. W.T. Grant Co.,* 416 U.S. 600, 94 S. Ct. 1895, 40 L. Ed. 2d. 406 (1974); *Boddie v. Connecticut,* 401 U.S. 371, 91 S. Ct. 780, 28 L. Ed. 2d 113 (1971).

These cases have been widely followed in the State Courts. See, e.g., *Blair v. Pitchess,* 5C. 3d 258, 280, 96 Cal. Rptr. 42, 486 P.2d 1242 (1971), *Laprease v. Raymours Furniture Company,* 315 F. Supp 716 (N.D.N.Y. 1970).

The taking effected by the automatic stay, wholly apart from the rights recognized by this Court in *Radford, supra,* is the *use* of the Petitioners' property — expressed either in terms of its inability to obtain the security for its loan or in terms of its inability to liquidate it.

The cases above cited establish beyond argument that the taking of petitioners' property without notice or opportunity to be heard — i.e., automatically — violated their right to due process.

Such a taking, in the case of a prejudgment wage garnishment, was held, in *Sniadach, supra,* to constitute an unconstitutional "taking of property without that procedural due process that is required by the 14th Amendment". 395 U.S. at p. 339.

Sniadach concerned the prejudgment garnishment of wages. Under the Wisconsin procedure, the clerk would issue a summons at the request of the creditors' lawyer, who would then serve the garnishee, freezing the debtor's wages unless or until the wage earner prevailed on the merits.

This Court, in holding the procedure unconstitutional, stressed the leverage the creditor may bring to bear upon the wage earner, pressure that "may as a practical matter drive a wage-earning family to the wall" (395 U.S. at 341) and concluded that where the taking was so obvious, it was easy to say that due process requires notice and a prior hearing.

In his concurring opinion, Mr. Justice Harlan pointed out that the property taken was the *use* of the frozen funds during the pre-trial period.

The parallel to the Chapter XII secured creditor situation is striking. Again, one side obtains cachet, without judicial scrutiny or review, to take the other's property. Again, it is done without notice or opportunity to be heard. And the effect, by shifting the risk to the creditor, is to *reverse* the leverage, so that the debtor, now safely hidden behind the

Bankruptcy Court's skirts, is able to make extortionate demands on his ever more desperate creditor.[50]

Whether the real estate lender may be driven "to the wall" is not as clear.[51] It is certainly not nearly as likely that becoming ensnared in a single Chapter proceeding will

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[50]A prominent recent example is the W.T. Grant Company Chapter XI proceeding. Grant, a nationwide retailer, closed over a thousand leased stores. Insulated from its landlords by the injunction, Grant discontinued paying rent on some of them and refused to pay use and occupation charges, although it retained its leasehold estates and declined to exercise its option to limit claims to three years' rent, pursuant to Rule 11-53, because to make such a motion would be "an administrative burden," (See Affidavit of Theodore Gewertz, dated February 6, 1976). As the months went by, many landlords — unable to deal with their own properties, having to pay on their own mortgages — were forced, by economic realities, to relinquish their rights to pre-Chapter rent due and unpaid, use and occupation payments, and damages. Grant tried to market the leases, with the Bankruptcy Judge conducting auctions in his courtroom. Many landlords ended up paying their tenant in order to recover their own property. One landlord paid $925,000. *In re W.T. Grant Company, supra.*

[51]There are currently three REITs in Chapter proceedings. They are Fidelity Mortgage Investors, with real estate investments of some $205,500,000; Continental Mortgage Investors, with real estate investments of $621,800,000; and National Mortgage Fund, with real estate investments of $64,100,000. (See *REIT's Monthly,* October 1976, National Association of Real Estate Investment Trusts, 1101-17th Street, N.W., Washington, D.C.)

Hampered by their non-liquidity, many other REITs are in default on their obligations to their bank lenders.

The number of "Problem Banks" on the Federal Deposit Insurance Corp. list is, in turn, growing. See *FDIC's Problem List Lengthens, Includes More Large Banks,* Wall Street Journal, November 4, 1976, p. 10.

have such effect. It must be borne in mind, however, that lenders have loans all across the country, and that the Bankruptcy laws are uniform throughout the United States (Article I, Section 8(4)).

The current situation is accurately summarized by Mr. Robert K. Lifton, in the introduction to his article "Real Estate in Trouble: Lender's Remedies Need an Overhaul", appearing in the Bicentennial issue of *The Business Lawyer* (July, 1976), at pages 1927-1930.

Lifton states:

"From one end of the country to the other real estate is in trouble. Aggressive overbuilding, sharply increased interest rates and an inflationary rise in the cost of building materials have hurt new construction. At the same time, properties generally are suffering from skyrocketing fuel and utility costs, rapid escalation of real estate taxes and a recessionary drop in demand for housing, office and commercial space. Defaults in construction loans on uncompleted buildings and in permanent mortgages on newly completed and even on heretofore successful properties are larger than in any time in our history. The possibility of massive losses on these loans threatens the viability of a number of lending institutions and seriously limits the ability of many others to provide sufficient credit, particularly for new construction, to fuel a strong economic recovery.

"The present state of the Real Estate Investment Trusts (REITs) and their bank lenders reflects the disaster in construction lending. Over 40 percent of the approximately $11 billion of construction loans held by the REITs are not meeting their payments. The REITs themselves borrowed most of their funds from large commercial banks. The nonearning loans held by REITs

substantially exceed the REIT's capital and subordinated debt and represent a good part of the assets supporting bank loans to the REITs. Estimates of losses to the bank lenders on these REIT loans range from $600 million to a shocking $1.8 billion. In addition to their loans to REITs, the commercial banks are saddled with their own portfolios of problem construction loans. So, too, are many savings and loan associations and savings banks.

". . . Faced with problem-ridden properties, both national and local builders have sought the protection of the bankruptcy laws and are tying up in protracted bankruptcy proceedings not only failing property but property that otherwise would be able to meet mortgage payments. Bankruptcy is also threatened for some of the larger REITs, many of which are staving off default only by swapping assets with their lending banks for cash and as debt repayment.

"If lending institutions are to maintain their stability in the face of the current real estate debacle, they must have effective remedies when default occurs that these remedies would at least permit them to limit their losses to manageable proportions. Lenders facing problems on uncompleted properties must have a speedy and inexpensive way of foreclosing on the properties and transferring them from weak hands to those capable of completing and operating them successfully. Even when a lender is prepared to inject new money into an unfinished project to complete it in a "work out" arrangement with the existing developer and contractors, it must have the leverage of being able to foreclose quickly so that it can compel a rapid resolution of the various parties' claims without being held up by any of the parties. Delays in work out or foreclosure of unfinished projects inevitably result in rapid deterioration of the property and escalating interest

and building costs over those originally estimated. Delay past completion dates specified in tenant leases may also permit tenants to walk away from lease commitments on which loans were predicated.

"When a mortgage on completed property goes into default, the mortgagee must be able to protect its security by making sure that whatever cash flow the property generates is used to pay real estate taxes and other operating expenses; to maintain the property in good condition; and to pay interest and amortization on its mortgage. The property should not be permitted to run down and the taxes and mortgage go unpaid while the debtor in possession "milks" the property using the income for his own purposes. When default continues, the lender in a reasonable time should be able to realize on its security and replace the existing management by foreclosing its mortgage. It can then sell the property to pay off its debt, place the property with a new mortgagor in whom it has more confidence or operate the property itself. For the REITs, the ability to clean up defaults means more viable properties to swap with their lenders for repayment of debt and working capital to keep them from the path of bankruptcy.

"State laws, both statutory and judicial, provide various remedies for the mortgagee to safeguard its security. But they also have developed elaborate rules to protect the defaulting debtor against being unfairly deprived of his property interest. Since these laws and decisions were developed in an era when the debtor requiring protection generally was a single family homeowner or small farmer, economically unable to stand up to a strong creditor, they frequently are biased in the debtors' favor. Although these particular debtors may still require greater protection, the bias built into the law is now benefiting commercial mortgagors who do not warrant special treat-

ment. Similarly, *the federal bankruptcy laws designed to provide a refuge for troubled debtors are currently being abused and offer the potential for even greater abuse by defaulting mortgagors.* As a result of both state and federal bankruptcy laws, lenders on commercial and multi-family residential real estate which goes into default must face unwarranted frustrating and time-consuming obstacles to the exercise of their remedies which not only increase their costs, but may destroy their property interests.

"In the last analysis, the system of real estate lending is based on confidence that the law will protect the lender's right to its security if the borrower defaults. Unless that confidence can be sustained through these difficult times, lenders will shy away from real estate loans in the future or so entrap them with restrictions that the real estate industry will not be able to operate effectively. The repercussions of a lagging real estate industry unable to satisfy housing or commercial needs will have detrimental social and economic implications for the nation.

"To foster the confidence of real estate lenders, state and federal legislators and courts should recognize that in many commercial real estate transactions, the pendulum of protection has swung too far in favor of the debtor. They should provide the momentum through corrective legislative and judicial action to start it swinging back towards the center." (footnotes omitted) (Emphasis added)

It is no answer to point out the provision of Rule 12-43 (d) giving priority to trial upon a complaint seeking relief from the stay, because that trial must obviously be held *after* the taking. And this Court has held that the opportunity for hearing must be *"before* he is deprived of any significant property interest," *Goldberg v. Kelley, supra.*

If it is unconstitutional for a creditor to sequester the property of a defaulting debtor, is it "equal protection" to allow the defaulting debtor to do so to his creditor? In the words of Congressman Gonzales, quoted by this Court in *Sniadich, supra,* "Where is the equity, the common sense, in such process?" 395 U.S. at 342.

In *Goldberg v. Kelley, supra,* this Court, in determining that a welfare recipient was entitled to notice and an opportunity to be heard before termination of welfare benefits which were statutory entitlements, weighed the conflicting interests, principally the fact that termination of aid might deprive an *eligible* recipient of the very means by which to live while he waits, and the important governmental interest in fostering the dignity and well being of all persons within its borders, against the countervailing governmental interests in conserving fiscal and administrative resources.

In the one asset, tax-shelter Chapter XII situation, this Court should balance the public interest in preserving that tax shelter and the "public benefit" of its rehabilitation (discounted by the likelihood of that event) as against the likelihood and extent of damage to the lender and its shareholders, policyholders, depositors or beneficiaries, the disruptive and chilling impact on the credit markets and the consequent effect on the national economy, and the potential liability of the United States for the creditors' loss.[52]

B. THE AUTOMATIC STAY IS UNCONSTITUTIONAL AS APPLIED AGAINST SECURED CREDITORS, BECAUSE ITS EFFECT IS TO TAKE THEIR PROPERTY WITHOUT ADEQUATE SAFEGUARDS FOR JUST COMPENSATION.

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[52]*Infra,* Point V, p. 75.

As previously discussed, the automatic stay operates as a taking of the use of Petitioner's property (*Sniadach, supra; United States v. Causby* 328 U.S. 256, 66 S. Ct. 1062, 90 L. Ed. 1206 (1946)) as well as those property rights enumerated in *Radford, supra.*

The threatened manner of imposing the "cram-down" creates a new dimension — even apart from the direct taking implicit therein — and that is this: the *probability* of loss (of interest, of monies paid out, such as for taxes) which existed at the outset is converted to a *certainty.*

It must be pointed out that where this Court has upheld prejudgment takings against Due Process challenges, it has done so because in those instances the party suffering the taking was completely protected. Thus, in *Mitchell v. W. T. Grant, supra,* where the Louisiana statute required an initial showing be made to the judge, a sufficient bond, a provision for immediate dissolution unless the sequestering party can prove the grounds upon which the writ was issued, and a method for recovering the property sequestered by posting a bond, this Court said:

> "Here, the initial hardship to the debtor is limited, the seller has a strong interest, the process proceeds under judicial supervision and management and the prevailing party is *protected against all loss.*" (Emphasis added) 416 U.S. at 618.

Absent the taking threatened by the "cram-down," the argument favoring the validity of the automatic stay is that it is merely a delay affecting Petitioners' remedies — a moratorium, of sorts.

Even if this were true, there is ample precedent against which to measure the argument, and it fails to measure up.

During the Depression of the 1930's, many states enacted mortgage moratorium laws to cope with the financial

emergency then prevailing. Generally, where the moratorium operated as the automatic stay does here, it was invalidated. Where the moratorium was conditioned on protecting the creditor, it was upheld.

The cases have been summarized in 59 *C. J. S.* § 505, p. 808:

> "It has been held that a mortgage moratorium statute providing for an automatic stay of foreclosure without compensation to the mortgagee is invalid, but that a statute authorizing the court in its discretion to grant a continuance in a mortgage foreclosure action, in proper cases, on conditions protecting the mortgagee's rights, and compensating him for the delay is valid, except as applied to actions pending when the statute is enacted."

The moratorium laws have fared no different in this Court. *Home Building and Loan Association v. Blaisdell, supra,* was a 5-4 decision wherein this Court, over a vigorous dissent, upheld the Minnesota Mortgage Moratorium Law, holding that it was not invalidated by the Contracts Clause (Article I, Section 10). The two principal reasons why the statute was upheld were the fact that it was limited to the duration of the declared emergency and the fact that it protected the mortgagee.

After reviewing the so-called "rent cases," this Court concluded that the Minnesota law was a reasonable exercise of the police power because:

1. An emergency existed in Minnesota;

2. The statute had a legitimate end;

3. In order to be constitutional, the relief had to be of a character appropriate to the emergency "and could be granted only upon reasonable conditions." (290 U.S. at 445); and

4. The conditions were not unreasonable. Under the statute, *the integrity of the mortgage indebtedness was not impaired;* interest continued to run; the right to sell, obtain title and obtain deficiency judgments was preserved; the conditions of redemption were unchanged; and *the mortgagor was required to pay the rental value of the premises,* such to be applied to the carrying of the property and to interest on the debt.

Compare the moratorium imposed by the automatic stay. The conditions found to be essential in *Blaisdell* — or any sort of equivalent — are nowhere to be found.

Some years after *Blaisdell, supra,* this Court decided *East New York Bank v. Hahn,* 326 U.S. 23, 66 S. Ct. 69, 90 L. Ed. 34 (1945).

The State of New York had also enacted a moratorium law. That legislation, first enacted in 1933, suspended the right of foreclosure for one year, but *obligated the mortgagor to pay taxes, insurance, and interest.* The moratorium was extended annually, (except for a two-year extension in 1941) but the legislature, responding to changing economic conditions, imposed the further condition that the principal be amortized at a rate of 1 percent (1942), then 2 percent (1944) and 3 percent (1945).

The challenge was based on the Contracts Clause and this Court, following *Blaisdell, supra,* rejected it, finding the protections afforded, and the frequent reconsideration of them, to constitute legislation at its fairest. The situation was not, the Court pointed out, like that of *W. B. Worthen Co. v. Kavanaugh,* 295 U.S. 56, 55 S. Ct. 555, 79 L. Ed. 1298, 97 A.L.R. 905 (1934).

The present case — particularly in view of the threatened "cram-down" — is like *Worthen,* where Arkansas statutes

had so altered mortgagees' remedies that Mr. Justice Cardozo was moved to comment:

> "Not even changes of the remedy may be pressed so far as to cut down the security of a mortgage without moderation or reason or in a spirit of oppression. Even when the public welfare is invoked as an excuse, these bounds must be respected. . . . With studied indifference to the interests of the mortgagee or to his appropriate protection they have taken from the mortgage the quality of an acceptable investment for a rational investor." 295 U.S. at 60.

The Arkansas statute lengthened the time required to foreclose from approximately 65 days to at least 2½ years, and possibly much longer. It reduced a 20 percent penalty to 3 percent and took away the mortgagee's right to collect costs and attorneys fees and to take possession after the sale and collect the rents and profits during the four-year redemption period. In case the mortgagee was displeased by all of this, the provision for expedited appeals was repealed.

The mortgagee was thus to be held off a minimum of 6½ years, although

> "Relief is not conditioned upon payment of interest and taxes or the rental value of the premises. The case is one of postponement for a term of many years with undisturbed possession for the debtor and without a dollar for the creditors." 295 U.S. at 61.

It didn't matter whether one or more of the charges could be upheld if considered separately, because the underlying reality was that they had a cumulative significance. "So viewed," Mr. Justice Cardozo said, "they are seen to be an oppressive and unnecessary destruction of nearly all the incidents that give attractiveness and value to collateral security." 295 U.S. at 62.

Mr. Harry H. Peterson, Attorney General of Minnesota, who had successfully argued in favor of the moratorium law in *Blaisdell, supra,* was again on the respondents brief in *Louisville Joint Stock Land Bank v. Radford, supra.* The difference was that *Radford* involved an Act of Congress — the Frazier-Lemke Act, an act designed to prevent farmers from losing their farms during the Depression of the 1930's. This Court was urged to follow *Blaisdell,* the argument being that if the Act was a bankruptcy law "The Fifth Amendment is inapplicable." 259 U.S. at 569.

The other principal difference was that the case was decided on Fifth Amendment, rather than Contract Clause grounds.

The Fifth Amendment provides that

> "No person . . . shall be deprived of life, liberty, or property without due process of law; nor shall private property be taken for public use without just compensation."

Radford held the bankruptcy power of Congress to be subject to the Fifth Amendment. Mr. Justice Brandeis, reviewing the history of the effect of bankruptcy and moratorium legislation upon mortgagees' rights, began by observing:

> **"This right of the mortgagee to insist upon full payment before giving up his security has been deemed of the essence of a mortgage."** 295 U.S. 555, at 580.

No act, prior to Frazier-Lemke, had "sought to compel the holder of a mortgage to surrender to the bankrupt either the possession of the mortgaged property or the title, so long as any part of the debt thereby secured remained unpaid. . . . No bankruptcy act had undertaken to supply him capital with which to engage in business in the future."

Comparing the mortgagees rights under the law of Kentucky with those substituted by Frazier-Lemke, the Court found the latter insufficient.[53] The answer, then, to the question "whether the Frazier-Lemke Act as applied here has taken from the Bank without compensation, and given to Radford, rights in specific property which are of substantial value."[54] (295 U.S. at 601) was "yes." The Act, accordingly, was unconstitutional.

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[53]The mortgagee could consent to a sale to the mortgagor at a so-called appraisal value. There was no down payment or any assurance the deferred payments would be made. Even if they were, the sale would not be at the appraised value because "the value of money (even if there were no risk) is obviously more than one percent." 295 U.S. at 591. And the value of the property was subject to continuing deterioration due to waste or accruing liens, such as taxes.

If the mortgagee refuses the above option, the mortgagor gets possession for 5 years with an option to purchase at a reappraised value at any time within the period (which gave the mortgagor a 5-year option to take advantage of any market softness with no risk — the mortgagee, meanwhile was precluded from accepting any offers made while market prices were high).

[54]The rights taken were:

"1. The right to retain the lien until the indebtedness thereby secured is paid.

"2. The right to realize upon the security by a judicial public sale.

"3. The right to determine when such sale shall be held subject only to the discretion of the Court.

"4. The right to protect its interest in the property at such sale wherever held, and thus to assure having the mortgaged property devoted primarily to the satisfaction of the debt, either through receipt of the proceeds of a fair competitive sale or by taking the property itself.

"5. The right to control meanwhile the property during the period of default, subject only to the discretion of the court, and to have the rents and profits collected by a receiver for the satisfaction of the debt." 295 U.S. at 594.

Radford is particularly compelling in the present case, for two reasons:

1. The same rights taken by Frazier-Lemke are being taken from Petitioners by the combined effect of the automatic stay and the "cram-down"; and

2. In passing Frazier-Lemke, Congress was careful to limit it to existing mortgages, because to make it applicable to future mortgages would destroy the possibility of the farmer obtaining mortgage credit.[55]

The concern expressed by Congress on the latter point is no less applicable in the present circumstance because, in the words of Professor Moo,

"There is an old adage in the credit business that there is *never* a high enough rate of interest or charge nor ever enough collateral available to make a bad loan,"[56] (Emphasis added)

and the automatic stay, coupled with the proposed use of the "cram-down" makes real estate "secured" loans "bad" because they encourage default, waste, and dishonesty, by giving the borrower the ability, decried by this Court in *Radford*, of taking advantage of the depressed value of the property — whether caused by market conditions or the borrowers own conscious or unconscious efforts — to

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[55]See comments footnoted at 295 U.S. 545:

"Senator Fess: ' . . . we may be making it impossible for the farmer in the future to borrow money.' "

"Representative Peyser: ' . . . you are removing from the farmer the possibility of securing any mortgage assistance in the future. I believe in the enactment of this law and the sealing down of values you are going to take away the possibility of help that may be needed by these farmers in the future.' "

[56]Moo, *The Secured Creditor in Bankruptcy*, p. 25.

"steal" it for a fraction of the money originally borrowed for its purchase or construction. Thus the retired mine worker, whose Pension Fund has invested in mortgages because of their security, might well suffer a reduction in his pension check, so that some defaulting borrower's right to avoid taxes might be preserved.

Petitioners contend that the automatic stay can only be constitutionally imposed if coupled with conditions adequate to protect the mortgagees from loss. Had Pinegate Associates, Ltd., attempted to enjoin Petitioners' foreclosure sale in either the state[57] or federal Court,[58] a bond would have been required.

Absent the sort of protections this Court has historically required, there is no public policy which justifies imposing the risk of loss — almost a certainty where, as here, the debtors one asset is worth less than the debt encumbering it — upon the lender in order to nourish the borrower's dreams of "rehabilitation".[59]

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[57]Georgia Code Annotated § 81A-165C.

[58]F.R.C.P. 65(1).

[59]"The presumption that 'time will heal' is simply not valid where the debtor has virtually nothing to reorganize except a single mortgaged project, especially where, as is the usual case, the rents are assigned or pledged and such pledges can probably now be made effective to withstand bankruptcy. Stays against secured creditors of single-project corporations rarely increase the probability of reorganization and consequently cannot further any policy aimed at enhancing all opportunities for success by the debtor.

"The practical price to the public involved in imposition of stays assumes greater significance when viewed against a general commercial setting. During the period of a stay, which in the case of mortgage loans may be extensive, creditors usually collect neither principal nor interest. A number of mortgage loan defaults in a period of economic stress could substantially interrupt the cash-flow pattern of the lender and impair its capacity to pay competitive dividend or interest rates." Daniel C. Draper, "Stays of Mortgage Foreclosure — A Proposal for Reform," *Banking Law Journal*, Spring 1976.

"[T]he Fifth Amendment commands that, however great the nation's need, private property shall not be thus taken even for a wholly public use without just compensation. If the public interest requires, and permits the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain; so that, through taxation, the burden of the relief afforded to the public interest may be borne by the public." *Radford, supra*, 295 U.S. at 602.

The purpose of Frazier-Lemke was to protect farmers, whose plight was considered to be dangerous to the entire nation. Accordingly, Frazier-Lemke was amended to include protections for the mortgagee. As amended, it was upheld. *Wright v. Vinton Branch of the Mountain Trust Bank*, 300 U.S. 440, 57 S. Ct. 556, 81 L. Ed. 736 (1937).

The amendment to Frazier-Lemke required any appraisals to be at the present fair market value and limited the duration of the stay to three years. If the debtor failed to comply with conditions imposed on him at any time, or if the debtor was unable to refinance himself within three years, the court could order the property sold. The *stay was conditioned upon the payment of the reasonable rental value* and the court could, in addition, require payments to be made on the principal and could, to further protect the creditors from loss, order unexempt personal property not necessary for the debtors farming operations sold.[60]

Under the Constitution, if private property is to be taken, it can only be done with the payment of just compensation. Absent payment, the *sine qua non* would clearly seem to be either sufficient protection against all loss, or eventual liability by the Federal government.[61]

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[60]Act of August 28, 1935, Ch. 792, § 6, 49 Stat. 943-45.

[61]*Infra*, point V.

One more analogy should be briefly noted: If the debtor-mortgagor retaining the property were, instead, a tenant; and if the mortgagee were his landlord, it is well established that the debtor would have to pay for the use and occupation of the premises during the Chapter proceedings. *Nat'l Levy & Co.*, 6 F.2d 970 (2d Cir. 1925); *120 Wall Associates v. Schilling*, 266 F.2d 548 (2d Cir. 1959); *In re United Cigar Stores Co.*, 69 F.2d 513 (2d Cir. 1934); *4A Collier on Bankruptcy* ¶70.44(4). Often, Chapter Petitions are filed the day before foreclosure — the day before the mortgagee, in most cases, would become the owner and the mortgagor a non-paying "tenant."

Does the Constitution sublimate form to the extent that substance must be ignored? A debtor in possession of mortgaged property should be required to pay the fair value of its use no less than a debtor in possession of leased property.[62]

IV. THE PROPOSED USE OF THE "CRAM DOWN" PROVISION OF BANKRUPTCY ACT SECTION 461 (11) TO TAKE REAL PROPERTY SECUR-

[62]See, for example, Murphy, *Restraint and Reimbursement: The Secured Creditor in Reorganization and Arrangement Proceedings*, 30 Business Lawyer 15 (1974) at pp. 32-38, wherein the author explores the deficiencies of *In Re Yale Express System, Inc.* 250 F. Supp. 249 (S.D.N.Y. 1966); 370 F.2d 433 (2d Cir. 1966) and 384 F.2d 990 (2d Cir. 1967), which denied a creditor secured by the debtors' trucks any use of rental payments. The article discusses *In Re Bermec Corporation*, 445 F.2d 367 (2d Cir. 1971), in which the secured creditor *was* paid the economic depreciation of the debtors' trucks, and several additional cases, including conditional sale cases, where payment was required. In *In Re Sun Cab Co.*, 67 F. Supp. 137 (D.C. Colo. 1946), for example, the Court recognized

> "It does not appear equitable to permit the debtor corporation to retain possession of the taxicabs, continue its business, while the taxicabs are depreciating, and fail to pay the balance due on the vehicles, shifting the risk of loss to the vendors." 67 F. Supp. at 139.

ING RESPONDENT'S DEBT TO PETITIONERS IS UNCONSTITUTIONAL. TO BE ADEQUATELY PROTECTED, PETITIONERS MUST EITHER RECEIVE THE REAL PROPERTY SECURING THEIR LOAN OR HAVE THE LOAN REPAID IN FULL.

Bankruptcy Judge Norton proposes to hold a hearing, at which he will "determine" the value of the security for Petitioners' debt, reasoning that, since Petitioners must look to the security for repayment, the "value of the debt", which must be adequately protected under Section 461(11)[63], is equal to the value of the security. That being done, Petitioners, according to the plan, will be paid the amount so determined in full satisfaction of their debt and their lien will be discharged, Pinegate Associates, Ltd. keeping the property and paying the creditors of the other five classes (most of whose claims would be worthless outside the bankruptcy court) up to 75% of their debts.

The plan states that this will be accomplished by either selling or refinancing the partnership's sole asset and by using the proceeds from the operation of the project during the Chapter XII proceedings.

The rents, issues and profits of the property are, however, subject to Petitioners' security interest. Any such use would constitute yet another taking of their property in derogation of the Fifth Amendment proscription.[64]

[63]11 U.S.C. § 861(11).

[64]Bankruptcy Judge Norton's Opinion, stating petitioners have not been treated inequitably thus far, points out:

> "By order of this Court dated March 20, 1976, the gross rent receipts less necessary operating expenses are paid to the creditor. . ." Appendix J, page 28 (footnote 40)

Actually, the order stated, "Plaintiffs' motion for sequestration of rents and profits is hereby DENIED." The debtor was ordered to invest the funds and hold the income subject to further orders of the Court. Appendix E, page 8.

This Court should prohibit the attempt to so "cram down" on Petitioners a repayment of less than the amount owed in compensation for the taking of their property because the scheme is obviously unworkable and can only result in further delay and, with the delay, further damage to Petitioners.

The scheme is unworkable for many reasons. Among them:

1. Bankruptcy Judge Norton's conclusion that the "value of the debt" is equal to the value of the apartment building is *clearly* erroneous;

2. Bankruptcy Judge Norton's conclusion that the scheme is feasible and in the best interests of the creditors is *clearly* erroneous; and

3. Such a scheme would be in conflict with the guarantees of the Fifth Amendment.

FIRST: Bankruptcy Judge Norton stresses that the Deeds to Secure Debt contain an "exculpatory clause".[65] Therefore, he reasons, Petitioners have limited themselves to looking to the value of their security to satisfy their debts.[66] Thus, according to Judge Norton, although Petitioners might be owed nearly 1.5 million dollars, if the real property is worth less than that, then the value of the debt is correspondingly less.

The constitutional objections to Bankruptcy Judge Norton's conclusions will be discussed in THIRD point, *infra,* as if they were true. At this point, however, it must be pointed out that Petitioners' security consists not only of the Deeds to Secure Debt encumbering the apartment project,

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[65]Appendix K, page 2, 11.

[66]Appendix K, page 11.

but also a lien on all the rents, income, receipts, revenues, issues and profits "forever, or for such shorter period as hereinafter may be indicated." (none indicated)[6]

Bankruptcy Judge Norton, in his order denying Petitioners' motion to sequester rents,[68] stated:

> "If, upon a hearing on the merits, the debtor is able to show that the assignment of leases and rents in this case is in fact an assignment as 'additional security', as opposed to a present and unconditional assignment, the

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[67]Appendix D.

[68]Petitioners' motion was based on what clearly appears to be the law — the secured creditor's right to collect the rents, issues and profits may be perfected by means of a petition to sequester rents filed in the Bankruptcy Court. *In re Kings County Real Estate Corp.*, 67 F.2d 895 (2d Cir. 1933); *Denco Development Co. v. Community Savings & Loan Assn.*, 376 F.2d 548 (9th Cir. 1967); *Groves v. Fresno Guarantee Savings & Loan Assn.*, 373 F.2d 440 (9th Cir. 1967); *Investors Syndicate v. Smith*, 105 F.2d 611 (9th Cir. 1939); *Mortgage Loan Co. v. Livingston*, 45 F.2d 28 (8th Cir. 1930), *cert. denied*, 290 U.S. 685 (1933); 4A *Collier on Bankruptcy*, ¶ 70.16(7). The sequestration is effective as of the date the secured creditor files his petition for sequestration. *Groves v. Fresno Guarantee Savings & Loan Assn., supra; American Trust Co. v. England*, 84 F.2d 352 (9th Cir. 1936); *Investors Syndicate v. Smith, supra;* 4A *Collier on Bankruptcy*, ¶ 70.16(7).

Moreover, the sequestered rents, issues and profits cannot be used by the debtor for the payment of general expenses of administration. *American Trust Co. v. England, supra; Mortgage Loan v. Livingston, supra; In re Hull*, 311 F. Supp. 197 (E.D. Cal. 1930); *Durand v. NLRB*, 296 F. Supp. 1049 (W.D. Ark. 1969); or diverted to other creditors, *In re Pittsburg - Duquesne Dev. Corp.*, 482 F.2d 243 (3rd Cir. 1973). See also *Stewart v. Platt*, 101 U.S. 731, 25 L. Ed. 816, (1879); *In re Williams Estate*, 156 F. 934 (9th Cir. 1907); *Mills v. Virginia - Carolina Lumber Co.*, 164 F. 168 (4th Cir. 1908); *Pollack v. Sampsell*, 174 F.2d 415 (9th Cir. 1949).

> plaintiffs would not be entitled to any assignment of rents until they are able to show that the primary security, the apartment complex itself, is inadequate to pay the indebtedness."[69]

Having denied Petitioners' motion to sequester the rents, Bankruptcy Judge Norton now threatens to deny his own reasoning by allowing the debtor to use those rents to pay other creditors, even though the apartment complex may be insufficient to pay the Petitioners' debt and even though Petitioners' debt is secured by those rents "forever."

If the value of Petitioners' debt, then, is measured by the value of the security, the value of the debt must be the total of the value of the real property plus the value of the income from that property *until the debt is paid in full.*

By the bankruptcy court's *own reasoning,* Petitioners must be paid the total amount owed them if their security is to be taken and the debt discharged![70]

In addition, it must be remembered that Petitioners' debt is secured by *real property* — and that real property has long been regarded as *unique.* Petitioners' contractual limitation (ignoring, as the bankruptcy court does, the lien on the rents) is *not* limited to the *value* of the real property, but to the real property itself.

Their right is to cause the property to be sold at foreclosure *and to bid at that sale.* Asking a court of equity for leave to foreclose is analogous to asking for specific performance of a contract to purchase land — relief which is almost universally available in this country, because,

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[69]Appendix E, page 4.

[70]Suppose the real property were the only security. If oil were discovered on the property prior to the valuation hearing, would the value of the debt still be defined as the value of the security?

since the exact counterpart of any particular piece of real estate does not exist anywhere else in the world, damages are presumed to be an inadequate remedy. That is the law in Georgia, *Hancock v. Hancock,* 223 Ga. 481, 156 S.E. 2d 354 (1967); *Whitehead v. Dillard,* 178 Ga. 714, 174 S.E. 244 (1934); *Clark v. Cagle,* 141 Ga. 703, 82 S.E. 21 (1914), as well as most other jurisdictions in this country[71] — if not "every country inhabited by people of Anglo-Saxon origin."[72]

SECOND: Bankruptcy Judge Norton finds the proposed scheme feasible and in the best interests of creditors despite his seeming awareness of the practical difficulties involved. Raising the necessary cash, he points out, is difficult.

> ". . . The experience and observation of this Court has been that the debtor cannot generally come up with the cash to implement such a plan. Hence, as a practical matter, the difficulty factor is quite large upon the debtor to provide in cash the value of the debt under this alternative."[73]

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[71]For example, Minnesota.

> " 'It is elementary that land contracts in particular are specifically enforced, *inter alia,* because one who has contracted to purchase a particular tract of land cannot get its exact counterpart anywhere. *** It is a unique thing, not capable of being duplicated. It is in consequence as much a matter of course for a court of equity to decree specific performance (of a valid land contract) as it is for a court of common law to give damages for breach of such a contract.' Eaton, Eg. 527, 528. This reasoning has been followed. . ." *Mellin v. Woolley,* 103 Minn. 498, 115 N.W. 654 (1908).

See also 25 Ruling Case Law § 71, for numerous additional citations.

[72]*Clark v. Cagle, supra,* at 705.

[73]Appendix K, page 10.

Analysis shows the difficulty to be even greater than the Bankruptcy Judge imagines. Under the plan, there are two alternative sources for funds: refinancing or sale. If the latter method is employed, the property cannot be sold for more than the amount to be paid to Petitioners (unless sold for more than the amount owed to Petitioners), or Petitioners have not been adequately protected to the extent of the value of the property — as is required, even under the theory of the Bankruptcy Court. But if the entire proceeds of the sale *are* paid over to Petitioners, there will be *nothing* left to implement the plan.

The refinancing method would be even more difficult, because it would require the debtor to obtain 100% financing — a practical impossibility — and *still* would provide no means for implementing the plan. Since most lenders are limited, either by prudence or by statute, to loans of approximately 75% of value, in order to pay Petitioners 1.2 million dollars (as proposed in the plan), for example, the value would have to be approximately 1.6 million dollars. But if the value *is* 1.6 million dollars, Petitioners are entitled to be paid in full — even under the Bankruptcy Court's theory.[74]

From the above, it is crystal clear that the procedure proposed by Bankruptcy Judge Norton can only result in a failure to protect Petitioners to the full extent of the value of the property, or in an exercise of futility which will only increase and prolong the taking of Petitioners' property.

The whole point of the threatened use of the "cram down" here appears to be an attempt to force Petitioners,

[74]In this connection, *Collier* observes:

"As a matter of practical effect, the cash outlay needed to appraise out senior lienholders would in most cases be so great as to prohibit the use of the device towards that end, aside from questions of fairness or constitutionality." 5 *Collier on Bankruptcy*, ¶ 77.17, p. 548.

through the device of appraisal, to pay Respondent's debts to its other creditors. This was also attempted in *Preble v. Wentworth,* (1st Cir. 1936) 84 F.2d 73, *cert. den.*, 299 U.S. 575, 57 S. Ct. 39, 81 L. Ed. 424 (1936), a case under Bankruptcy Act § 77B, where seven classes of creditors assented to the debtor's plan and the first mortgage bondholders did not. The debtor then moved for an appraisal of the value of the non-assenting classes' interests and securities, with a view toward paying the appraised value for a discharge of the debt.

The District Court, in an opinion accepted, in turn, by the First Circuit and by this Court, refused to allow it. That opinion is particularly appropriate here:

> "'. . . to take the property from the mortgagee upon an appraisal is an attempt to use a supposed or possible value, over and above the appraisal, for the benefit of other creditors and stockholders. If there is any surplus value, it belongs to the first mortgagee up to the amount of his debt. If there is none, there is nothing to build on, and there would seem to be no object in having an appraisal in the absence of a disclosure of a method of raising the money, unless junior interests are prepared to advance the money on a chance of increased value in the future, and there is no information before the court to that effect. A plan cannot be called either fair or feasible which discloses no method or probability of being carried out unless, perchance, the appraisers make a mistake in valuation.'" 84 F.2d at 74.

Preble, of course, may be distinguished by pointing out that Chapter XII no longer[75] requires a plan to be "fair and

[75]Appendix K, p. 13, 14 (footnote 27).

While the words "fair and equitable" may have become "words of art," still it is unfortunate that the requirement that any judicial proceeding be *fair* and *equitable* should be removed from the law.

equitable." While this may be true, it hardly seems a creditable basis to justify Petitioners' being "ripped off" for the benefit of junior creditors. The Chapter XII plan must still be feasible, and the logic of *Preble* is still sound.

The Bankruptcy Court recognizes, however, that besides being feasible, the plan must also be in the best interests of "creditors."[76]

Which creditors? The Act defines "creditors" as "holders of claims"[77] and "claims" as "all claims of whatsoever character, against a debtor or his property."[78]

In the present instance, Petitioners are first lienholders whose claims constitute well over 90% of the claims against the debtor or its property. Under the law of Georgia, their claims are superior to those of most of the Respondent's other creditors. In the normal course, absent bankruptcy proceedings, these other creditors would get nothing.

Upon entering the Kafkaesque world of Chapter XII, as envisioned by Bankruptcy Judge Norton, however, these relationships are suddenly turned topsy-turvy. Petitioners' rights are no longer paramount, but instead are subject to the desires of the subordinate lienholders and even unsecured creditors. This small minority of less than 10% (including, here, one of Respondent's general partner's other ventures, and his wife) can vote to tax the Petitioners, in effect forcing them to pay the debtor's debts to the others — despite the fact that there is no relationship between Petitioners and the other creditors.

In the single asset Chapter XII, where the single asset is worth less than the first lien, the remaining creditors will

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[76]Appendix K, p. 13.

[77]§ 406(5) (11 U.S.C. 806(5)).

[78]§ 406(2) (11 U.S.C. § 806(2)).

always approve a plan designed to take the first lienholder's property and give it to them.[79] As a nation, we have applauded the concept (in Robin Hood), rejected it (in Marx and Mao), and *prohibited it* (in the Fifth Amendment).

The extreme minority-rule concept cannot be justified in terms of democracy,[80] but only in terms of egalitarianism — a concept that, while increasingly popular,[81] has never been imported to the law of secured transactions to disrupt its established priorities.

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[79]This proposition has not escaped judicial comment. See *Kyser v. MacAdam* (2d Cir. 1941) 117 F.2d 232, at 238:

> "If an arrangement is to be adopted through vote of the unsecured creditors alone on the theory that the secured creditors are not affected, since their claims have been devalued to the value of the security, then control of the arrangement will by this device be always thrown into the hands of the unsecured creditors."

[80]Cf. *Baker v. Carr*, 369 U.S. 186, 82 S. Ct. 691, 7 L. Ed. 2d 633 (1962).

[81]See "Egalitarianism: Threat to a Free Market", *Business Week*, December 1, 1975, p. 62; "Egalitarianism: Mechanisms for Redistributing Income," *Business Week*, December 8, 1975, p. 86; "Egalitarianism: The Corporation as Villain," *Business Week*, December 15, 1975, p. 86.

> "The egalitarian movement is essentially authoritarian. It is highly critical of business and contemptuous of laissez-faire economics.
>
> "Business for its part sees the egalitarian push as a threat not just to its pay scales but to the fundamental principles of a market economy. It is right. The American economy, based on private property, uses the market to determine rewards and allocate resources. Differences in pay and profit are essential to it. At some point, therefore, a move toward equality would require a shift from capitalism to a socialist or government-directed state. By all indications, the U.S. is still a long way from this point. But the inherent contradiction between a political democracy and a capitalist economy has yet to be resolved." *Business Week*, December 1, 1975, page 62.

The manifest result of validating the procedure threatened by Judge Norton would be to encourage not only waste, but fraud. Suppose, for example, a debtor borrows two million dollars to buy or build income-producing property. Why shouldn't he "milk" the property, defer maintenance, siphon off the income, then file Chapter XII, have the property appraised at its then depressed value — say $750,000 — and then "steal" it?

THIRD: Bankruptcy Judge Norton's Opinion relies upon this Court's decision in *Wright v. Union Central Life Insurance Co.*, 311 U.S. 273, 61 S. Ct. 196, 85 L. Ed. 184 (1940) — another Frazier-Lemke case — to avoid the requirements of *Louisville Joint Stock Land Bank v. Radford, supra.*

The *Wright* opinion modified a judgment ordering the sale of a farmer-debtor's property, with the mortgagee permitted to purchase at the sale and the mortgagor entitled to redeem at the purchase price plus 5% interest, as provided by the Act. The modification made that sale subject to the prior right of the farmer to first have the property reappraised, then have a reasonable opportunity to redeem at the appraisal price.

Reviewing the two provisos appended to § 75(a)(3),[82] Mr. Justice Douglas found them both to be mandatory, rather than considering the first qualified by the second. To reconcile "these seemingly inconsistent remedies," he looked to the purpose of the Act — "to effectuate a broad program of rehabilitation of distressed farmers faced with the disaster of forced sales and an oppressive burden of debt." (311 U.S. at 278)

[82]Section 75(a)(3) of the Frazier-Lemke Act provided: "(3) At the end of three years, or prior thereto, the debtor may pay into court the amount of the appraisal of the property of which he retains possession, including the amount of encumbrances on his exemptions, up to the amount of the appraisal, less the amount

The provision that, if at any time the debtor fails to comply with the provisions of the section or the orders of the court, or is unable to refinance within three years, the court could order a sale, was apparently held to be meaningless upon the ground that it was inconsistent with the right to redeem at the reappraisal value. A confusing passage states that Congress was provided the above power, but the Court could not *infer* that they meant what they *said*. To so hold, the opinion states, would be to *imply* a power wholly inconsistent with the aim of aiding and protecting farmer-debtors, and "such an important remedial right cannot be lost by mere implication." 311 U.S. at 281

Of course, this fails to take into account the fact that the language was *in the statute* and did not need to be implied, and that it was there for good reason — Congress was required to amend Frazier-Lemke to provide safe-

paid on principal: *Provided,* That upon request of any secured or unsecured creditor, or upon request of the debtor, the court shall cause a reappraisal of the debtor's property, or in its discretion set a date for hearing, and after such hearing, fix the value of the property, in accordance with the evidence submitted, and the debtor shall then pay the value so arrived at into court, less payments made on the principal, for distribution to all secured and unsecured creditors, as their interests may appear, and thereupon the court shall, by an order, turn over full possession and title of said property, free and clear of encumbrances to the debtor: *Provided,* That upon request in writing by any secured creditor or creditors, the court shall order the property upon which such secured creditors have a lien to be sold at public auction. The debtor shall have ninety days to redeem any property sold at such sale, by paying the amount for which any such property was sold, together with 5 per centum per annum interest, into court, and he may apply for his discharge, as provided for by this Act. If, however, the debtor at any time fails to comply with the provisions of this section, or with any orders of the court made pursuant to this section, or is unable to refinance himself within three years, the court may order the appointment of a trustee, and order the property sold or otherwise disposed of as provided for in this Act."

guards for secured creditors after this Court found the Act unconstitutional in *Radford, supra.*[83]

Nonetheless, Mr. Justice Douglas, in the passage relied upon by the bankruptcy court, recalled that, while the Act was to provide a broad program to aid distressed farmers,

> "Safeguards were provided to protect the rights of secured creditors, throughout the proceedings, to the extent of the value of the property. *John Hancock Mutual Life Ins. Co. v. Bartels, supra,* at pp. 186-187; *Borchard v. California Bank, supra,* at p. 317. There is no constitutional claim of the creditor to more than that." 311 U.S. at 278

Both of the cases cited in the quoted passage were decided on procedural grounds. *Borchard* (310 U.S. 311, 60 S.C. 957, 89 L. Ed. 1222 (1940)) was, essentially, a case of invited error, wherein the bank had resorted to a procedure not contemplated by the statute and this court held the petitioner-debtors entitled to compliance with the statutory procedure. *John Hancock* (308 U.S. 180 59 S. Ct. 794, 83 L. Ed. 1498, (1939)) was a case where the debtor had followed the statutory procedure, but the Court had not. (The Court dismissed the petition because there was no reasonable probability of the debtor's financial rehabilitation. The Act provided no procedure for dismissal on that ground.) By stipulation, the Bank had apparently obtained an advantage over the farmer, who never did get the stay order he was entitled to under the

[83]Collier suggests that, out of sympathy for the farmer whose extreme plight was regarded as dangerous to the welfare of the nation as a whole, the Court in *Wright v. Union Central* went further than it would be willing to go in a reorganization case to advance junior interests. "No such sympathy," *Collier* says, "would be present to tip the balance in a contest between senior and junior interests in reorganization. An authoritative answer, however, remains to be given on this point. . ." 5 *Collier on Bankruptcy,* ¶ 77.17, p. 546.

Act. This Court clearly stated that it was only concerned "with the duty to follow the procedure which the statute defines and the District Court failed to observe." 308 U.S. at 187.

Both cases observed that, in the scheme of the statute, *the priorities and liens of secured creditors were preserved.* They were entitled, therefore, to the "fair and equitable" treatment *which has been removed from Chapter XII.*

In view of this Court's previous decisions upholding emergency-related legislation to protect farmers (cf. *Home Building & Loan Assn. v. Blaisdell, supra)*, it would be reasonable to believe that the "that" that the creditor could constitutionally claim is really "safeguards" rather than "the value of the property." Certainly, such interpretation would harmonize the *Wright* decision with the other great decisions of this Court, including *Blaisdell, supra,* and *Radford, supra.*

This conclusion is buttressed by the language of Section 453 of Chapter XII (11 U.S.C. § 853), which provides, in part:

> "For the purposes of the classification [of creditors according to the nature of their claims], the court shall, if necessary . . . fix a hearing upon notice to the holders of secured claims, the debtor, the trustee . . . to determine summarily the value of the security *and classify as unsecured the amount in excess of such value.*"

See, also, § 197 (11 U.S.C. 597) (Chapter X), § 57(h) (11 U.S.C. § 93(h)) and Rule 306(d).

Under § 453, if the security is worth less than the debt, the creditor may participate with the unsecured creditors with regard to the debtor's other assets, if any. See 9 *Collier on Bankruptcy,* ¶ 7.03, p. 1013. So even though the creditor's constitutionally protected *security*

may be limited to the property, his *claim* is not. To discharge the lien and the debt upon payment of the value of the security would deny the creditor any further claim, even as an unsecured creditor.

Petitioners suggest that *Collier* is right: that this Court extended special protection to farmers in *Wright* that would then, and should now, be unavailable to debtors such as Respondent herein. Petitioners suggest that the farmer's plight — as evidenced by the rapidity with which Congress amended Frazier-Lemke after *Radford* — caused Mr. Justice Douglas to seek an interpretation that would preserve the Act. Thus, the first proviso, which allowed any secured *or unsecured* creditor (or the debtor) to request a reappraisal, protected the parties who might have claim to the residual value in a situation where the original appraisal was below market value, but sufficient to pay the prior encumbrance. The *second* proviso, which would seem, simply by its placement, to modify the *first* in the same manner that the first modifies the language that precedes *it*, gives to *secured creditors* the right to demand a public sale. Thus, the Act protects junior creditors where the original appraisal is sufficient to pay the senior creditor and protects the senior creditor where the reappraisal is less than his debt.

Petitioners submit that *Wright* is anomalous and should be restricted to the unique historical context in which it arose.

It is interesting to note that subsequent to the *Wright* decision, which effectively eliminated the second *proviso* of Section 75 (s)(3) as a modification of the first *proviso*, an attempt was made to limit the *first proviso* as a modification to Section 75 (s)(3).

In *In re Whitwer*, 44 F. Supp. 466 (D.C. Neb. 1942), a farmer debtor — represented by William Lemke, co-author

of the Frazier-Lemke Act — sought to redeem at the original appraisal, denying the secured creditor the right to a reappraisal, as provided in the first *proviso*. As pointed out in the Opinion, the same argument had unsuccessfully been made in *Wright* following its return from this Court to the District Court. The Circuit Court, in that case, had pointed out that it was easy to conceive of a case in that circuit where oil might be discovered on the property during the moratorium. In *Whitwer*, oil *had* been discovered and the debtor was insisting on his "right" to redeem property with a fair market value of Four Hundred Thousand Dollars for the original appraisal figure of Four Thousand Dollars!

The Court was aghast:

> "He is invoking the jurisdiction of this court not as a shield, but rather as a scourge. The allowance of his petition under the guise and in the name of the unfortunate would achieve the perversion of the very purposes of the amendment." 44 F. Supp. at 472.

The *Whitwer* case illustrates graphically why, if the debtor is unable to pay the secured creditor's debt in full, no "appraisal value" of that debt can be an adequate substitute for the real property itself.

The reasoning of the debtor in *Whitwer*, however, was not unlike that of Mr. Justice Douglas in *Wright*.

V. THE TUCKER ACT PROVIDES THE MEANS FOR ANY SECURED CREDITOR TO OBTAIN JUST COMPENSATION FOR PROPERTY TAKEN IN BANKRUPTCY PROCEEDINGS.

The philosophy of the Fifth Amendment is to protect the individual against the uncompensated taking of his property by his government. It does not say that private property may *not* be taken, nor has this court so held. It says that if it is to be taken, just compensation must be paid.

So understood, the principle has been upheld by this Court from the beginning. Thus, in cases such as *Radford, supra,* where property was taken without compensation *and without adequate safeguards to insure that compensation would be available,* the statute was held to violate the Fifth Amendment. In the moratorium cases, such as *Blaisdell, supra,* as well as the cases upholding the amended Frazier-Lemke Act, this Court refused to strike down the statutes involved *because adequate safeguards were provided.*

The same distinction can be found in the cases measuring state prejudgment attachment statutes against the Fourteenth Amendment. Compare, for example, *Sniadach, supra,* where there were no protections, with *Mitchell v. W. T. Grant Co., supra,* where this Court found the protections adequate. In the former case, the statute was struck down; in the latter, it was upheld.

The circumstances under which an individual may suffer his property to be taken by the United States are manifold. They range from the *Radford* situation, where compensation or protection was practically nonexistent, to the opposite extreme such as where the government buys the property through negotiations or condemnation proceedings.

Between those extremes, a large area has been carved out wherein actions taken pursuant to statutes which provide little, if any, safeguards for compensation, have resulted in the taking of property. This Court has upheld those statutes by *implying* the promise to pay for what was taken, thus making the Tucker Act[84] available to allow the individual damaged by the taking to proceed against the United States in the Court of Claims.

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[84]28 U.S.C. § 1491. See Appendix A.

United States v. Causby, supra, for example, was a case where government planes so scared a farmer's chickens that they destroyed the value of his property as a commercial chicken farm. This Court held the taking compensable in damages. *United States v. Dickinson,* 331 U.S. 745, 67 S. Ct. 1382, 91 L. Ed. 1789 (1947) and *Jacobs v. United States,* 290 U.S. 13, 54 S. Ct. 26, 78 L. Ed. 142 (1933) involved flooding and eroding of property caused by dams built by the government pursuant to Congressional authority. In both cases, this court found an implied promise to pay and, in the *Jacobs* case, held the just compensation impliedly promised entitled the owner to the value of the property taken *plus interest* from the time of the taking. In *Armstrong v. U.S.* 346 U.S. 40, 80 S. Ct. 1563, 4 L. Ed. 2d. 1554 (1960), mechanics' lien rights were taken when the United States exercised its contract right to take title from the prime contractor, making lien enforcement impossible because of sovereign immunity. In *Duckett & Co. v. U.S.,* 266 U.S. 149, 45 S. Ct. 38, 69 L. Ed. 216 (1924), possession of a lessee's leased property was taken pursuant to a statute authorizing the President to take possession of any system of transportation. None of the above were cases where the United States brought formal condemnation proceedings. (Cf. *Almota Farmers Elevator & Warehouse Co. v. U.S.,* 409 U.S. 470, 93 S. Ct. 791, 35 L. Ed. 2d. 1 (1972), where a leasehold was condemned and this Court held the condemnee also entitled to compensation for improvements). None of them was concerned with the determination of whether the underlying statute provided adequate safeguards — instead, the adequate safeguards were found in the availability of a procedure in the Court of Claims.

The synthesis of the Fifth Amendment prohibition, the moratorium/reorganization and the implied promise theories has finally been achieved in the recent *Regional Rail*

Reorganization Cases, 419 U.S. 102, 95 S. Ct. 335, 42 L. Ed. 2d. 320 (1974). Those cases involved the Regional Rail Reorganization Act, which required the assets of several railroads then in reorganization proceedings to be transferred to a new corporation (Conrail) in return for Conrail securities and a limited amount of federally guaranteed United States Railway Association (USRA) obligations. This was to be accomplished in accordance with a plan mandated to be formulated by USRA by July 26, 1975. Until that plan became effective, the railroads were generally unable to discontinue service or abandon any line which would become part of the consolidated railway system.

The largest of the eight railroads involved was the Penn Central Transportation Company ("Penn Central"). Various parties with interests in Penn Central attacked the constitutionality of the Rail Act on the grounds that it would take Penn Central property without just compensation in two ways: by *conveyance* — i.e., the transfer of assets compelled by the Act would not be adequately compensated for by the Conrail securities and USRA obligations; and by *erosion* resulting from the compulsory operation of money-losing lines required by the Act.

In an opinion called "a sheer *tour de force*" in Mr. Justice Douglas' dissenting opinion, this Court recognized the two forms of taking and found the issue of both to be ripe for determination.

Observing that

> "there are clearly grave doubts whether the Rail Act would be constitutional if a Tucker Act remedy were not available as compensation for any unconstitutional erosion not compensated under the Act itself," (419 U.S. at 134)

this Court held that the Tucker Act *was* available to provide just compensation for the erosion taking[85] and for the conveyance taking.[86] Having so held, this Court found the Tucker Act remedy to be adequate and, there being adequate safeguards to protect the right to just compensation, upheld the validity of the Rail Act.[87]

The availabiilty of the Tucker Act was based upon an implied promise to pay for the taking.

> "The general rule is that whether or not the United States so intended, '[i]f there is a taking, the claim is "founded upon the Constitution" and within the jurisdiction of the Court of Claims to hear and determine.' *United States v. Causby,* 328 U.S. 256, 267, 90 L. Ed. 1206, 66 S. Ct. 1062 (1946). '[I]f the authorized action . . . does constitute a taking of property for which there must be just compensation under the Fifth Amendment, the Government has impliedly promised to pay that compensation and has afforded a remedy for its recovery by a suit in the Court of Claims. *Yearsley v. Ross Construction Co.,* 309 U.S. 18, 21, 60 S. Ct. 413, 415 84 L. Ed. 554, (1940). See also *Hurley v. Kincaid,* 285 U.S. 95, 52 S. Ct. 267 76 L. Ed. 637, (1932). In *Yearsley,* the Court, speaking through Mr. Chief Justice Hughes, went on to hold that 'it cannot be doubted that

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[85]419 U.S. at 136.

[86]419 U.S. at 148.

[87]The availability of the Tucker Act was said to cure "what might otherwise be a troublesome problem of procedural due process" (419 U.S. at 156), because the complainants had *no interest in retaining the properties themselves* — they only wished to be made whole.

Petitioners herein assert that, absent complete repayment through the bankruptcy proceedings or through Tucker Act proceedings, they are entitled to the real property in which they have a security interest.

the remedy to obtain compensation from the government *is as comprehensive as the requirement of the Constitution . . .*' 309 U.S. at 22, 84 L. Ed. 554. (Emphasis supplied.)"

The situation underlying the *Rail Reorganization Cases* was not unlike that of the various mortgage cases discussed herein, because there was believed to be "a rail transportation crisis seriously threatening the national welfare." 419 U.S. at 108. Thus, the statute seeking to deal with the rail transportation emergency was upheld, just as this Court upheld the statute seeking to protect farmers in their hour of emergency more than three decades previously.

It must be noted, however, that Mr. Justice Douglas, the author of the opinion in *Wright v. Union Central Life Insurance Co., supra,* wrote the only dissenting opinion in the *Rail Cases.* Mr. Douglas, pointing out that this is the first time this Court has utilized the availability of the Tucker Act in order to uphold a reorganization or bankruptcy statute, would prefer to meet the challenge. Rather than doing so, he argued, the statute should be held unconstitutional.

> "Congress has lowered all the procedural barriers and foisted on these rail carriers a conveyance of their assets which, if done by private parties in control of a bankrupt estate, would be a fraudulent conveyance. Here it is achieved by Congress' purporting to act in the 'public interest.' That is a taking for a public purpose; but by Fifth Amendment standards it is a taking of property without assurance of just compensation." 419 U.S. at 167.
>
> "The construction the Court gives the Rail Act today will amaze the legislators who drafted and voted for this statute. I cannot believe that Congress would have enacted this law had it been told that in the end it might have to dig into taxpayers' pockets not for the one billion appropriated but for unknown billions — perhaps 10 to 12 billion — for 'just compensation' for property it authorized to be 'taken.' " 419 U.S. at 180.

Mr. Douglas pointed out, by way of footnote, that this Court could have utilized the Tucker Act in *Radford, supra,* to avoid having to declare the Frazier-Lemke Act unconstitutional.[88] This brings us full circle: the decision in the *Regional Rail Reorganization Cases* realizes the prophesy of Mr. Justice Brandeis, writing more than forty years ago:

> "If the public interest requires, and permits the taking of property of individual mortgagees in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain. So that, through taxation, the burden of the relief afforded to the public interest might be borne by the public." *Radford, supra,* 295 U.S. at 602.

Petitioners are subject to both conveyance and erosion takings herein. Their lien is to be discharged and the debt extinguished without having been fully paid, under the "evaluation" procedure of Section 461(11) — a conveyance taking. Moreover, Petitioners, restrained for almost a year now under the automatic stay, have suffered an erosion taking, both under Bankruptcy Judge Norton's "cram down" theory and in fact, because they have been required to finance the Chapter XII proceedings — to make an involuntary interest-free loan as well as to pay or have accrue liability for real property taxes, all the while being denied their right to the rents, issues and profits of the real property.

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[88]Footnote 17, 419 U.S. at 179.

Petitioners suggest that, while the availability of the Tucker Act might again be a sufficient basis for avoiding the Constitutional questions herein, the necessity for protecting the rail transportation system serving a major portion of this country during eight railroads' hour of crisis is not coextensive with that of protecting a tax-shelter partnership such as Pinegate Associates, Ltd. in *its* hour of crisis.

In the present case, Petitioners have already suffered nearly a full year's erosion taking, with no end in sight. The bankruptcy court has failed to accord Petitioners *any* safeguards to insure compensation for their loss. Accordingly, Petitioners' only source for the "just compensation" they are entitled to under the Constitution would appear to be the United States. While perhaps inevitable in this case, this result is not a very desirable one. The taxpayers should not be required to "bail out" speculative ventures created for the purpose of taking advantage of the tax laws. Rather, enjoined secured creditors should be provided adequate safeguards to protect against loss. The result would be to reserve Chapter XII to appropriate situations and eliminate its abuse, saving both time and money for the judicial system, the taxpayers, secured real property lenders, the entire credit market and, *a fortiori,* the national economy.

CONCLUSION

The abuse of Chapter XII proceedings is encouraged by the Rules of Bankruptcy Procedure. By surrendering the injunctive powers of the United States to the discretion of private individuals, the Rules threaten the disruption of the multi-billion dollar real estate industry. The validation of the proposed use of the cram down would threaten billions in existing loans and jeopardize the chances of any future borrowers' obtaining funds on terms approximating those available in the market place today. To read lenders' protection into Chapter XII via the Tucker Act would make the United States government an insurer of every loan.

Petitioners submit that this Court should grant the writs prayed for herein, preventing Petitioners from suffering further erosion losses, and requiring the provision of adequate safeguards as a condition to the maintenance of the stay against lien enforcement. Petitioners submit that, absent a willingness and ability on the part of the Respondent to at least pay its current obligations and protect Petitioners, there is no justification, under the Constitution, for continuing to restrain Petitioners from proceeding to enforce their lien.

Respectfully submitted,

JON R. MOSS
PAUL S. BERGER
Berger, Berger, Kahn & Shafton

ROBERT N. MEALS, JR.
E. PENN NICHOLSON
Nicholson & Meals

M. C. McLAIN
Counsel and Assistant Secretary
Great National Life Insurance Company

Attorneys for Petitioners

CERTIFICATE OF SERVICE

It is hereby certified that three (3) copies of the above and foregoing MOTION FOR LEAVE TO FILE PETITION FOR WRIT OF PROHIBITION AND/OR MANDAMUS AND/OR CERTIORARI TO THE DISTRICT COURT, NORTHERN DISTRICT OF GEORGIA, ATLANTA DIVISION and Appendices have been served upon the following persons by placing same in the United States mail, postage prepaid, this 26th day of November, 1976, addressed to the addresses set forth after the name of each:

1. Charles E. Campbell, Esq.
   Heyman and Sizemore
   300 Fulton Federal Bldg.
   Atlanta, Georgia 30303

2. William L. Norton, Jr.
   Bankruptcy Judge
   United States District Court
   Northern District of Georgia
   Atlanta Division
   56 Forsyth Street
   Atlanta, Georgia 30303

3. William C. O'Kelley
   United States District Judge
   United States District Court
   Northern District of Georgia
   Atlanta Division
   56 Forsyth Street
   Atlanta, Georgia 30303

4. Solicitor General
   Department of Justice
   Washington, D.C. 20530

APPENDIX A

APPENDIX A

CONSTITUTIONAL PROVISIONS, STATUTES AND RULES INVOLVED

Constitutional Provisions

1. The Fifth Amendment to the Constitution of the United States provides in pertinent part as follows:

> "No person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

2. Article I, Section 1 of the Constitution provides as follows:

> "Section 1. All legislative Powers herein granted shall be vested in a Congress of the United States, which shall consist of a Senate and House of Representatives."

3. Article III, Section 1 of the Constitution provides in pertinent part as follows:

> "The judicial Power of the United States shall be vested in one Supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish."

4. Article I, Section 8 of the Constitution provides in pertinent part as follows:

> "The Congress shall have Power . . . to establish . . . uniform Laws on the subject of Bankruptcies throughout the United States;"

Federal Statutes and Rules of Civil Procedure

1. Title 28 U.S.C. § 2075 provides, in relevant part:

> "The Supreme Court shall have the power to prescribe by general rules the forms of process, writs, pleadings

and motions, and the practice and procedure under the Bankruptcy Act.

"Such rules shall not abridge, enlarge or modify any substantive right . . .

"All laws in conflict with such rules shall be of no further force or effect after such rules have taken effect."

2. Federal Rules of Civil Procedure § 65(1) provides:

"No restraining order or preliminary injunction shall issue except upon the giving of security by the applicant, in such sum as the Court deems proper, for the payment of such costs and damages as may be incurred or suffered by any party who is found to have been wrongfully enjoined or restrained."

3. Tucker Act, 28 U.S.C. § 1491 provides:

"The Court of Claims shall have jurisdiction to render judgment upon any claim against the United States founded either upon the Constitution, or any Act of Congress, or any regulation of an executive department, or upon any express or implied contract with the United States, or for liquidated or unliquidated damages in cases not sounding in tort."

Bankruptcy Act Provisions

1. Bankruptcy Act, Chapter XII, Real Property Arrangements By Persons Other Than Corporations, United States Code, Title 11, Chapter 12, §§ 801-926.

A. 11 U.S.C. § 861(11)(c):

"An arrangement — (11) shall provide for any class of creditors which is affected by and does not accept the arrangement by the two-thirds majority in amount required under this chapter, adequate protection for the realization by them of the value of their debts against

the property dealt with by the arrangement and affected by such debts, either, as provided in the arrangement or in the order confirming the arrangement, (a) by the transfer or sale, or by the retention by the debtor, of such property subject to such debts; or (b) by a sale of such property free of such debts, at not less than a fair upset price, and the transfer of such debts to the proceeds of such sale; or (c) by appraisal and payment in cash of the value of such debts; or (d) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection;"

B. 11 U.S.C. § 828:

"Unless and until otherwise ordered by the court, upon hearing and after notice to the debtor and all other parties in interest, the filing of a petition under this chapter shall operate as a stay of any act or proceeding to enforce any lien upon the real property or chattel real of a debtor."

C. 11 U.S.C. §823:

"A petition filed under this chapter shall state that the debtor is insolvent or unable to pay his debts as they mature, and shall set forth the terms of the arrangement proposed by him."

D. 11 U.S.C. § 806(9):

"(9) 'petition' shall mean a petition filed under this chapter proposing an arrangement by a debtor.' "

Rules of Bankruptcy Procedure

1. Rules of Bankruptcy Procedure, Rule 12-43:

"(a) Stay of Actions and Lien Enforcement. A petition filed under Rule 12-6 or 12-7 shall operate as a stay

of the commencement or the continuation of any court or other proceeding against the debtor, or the enforcement of any judgment against him, or of any act or the commencement or continuation of any court proceeding to enforce any lien against his property, or of any court proceeding for the purpose of the rehabilitation of the debtor or the liquidation of his estate.

"(*d*) *Relief from Stay.* On the filing of a complaint seeking relief from a stay provided by this rule, the bankruptcy court shall, subject to the provisions of subdivision (c) of this rule, set the trial for the earliest possible date, and it shall take precedence over all matters except older matters of the same character. The court may, for cause shown, terminate, annul, modify or condition such stay. A party seeking continuation of a stay against lien enforcement shall show that he is entitled thereto.

"(*e*) *Ex Parte Relief from Stay.* On the filing of a complaint seeking relief from a stay against any act or proceeding to enforce a lien or any proceeding commenced for the purpose of rehabilitation of the debtor or the liquidation of his estate, relief may be granted without written or oral notice to the adverse party if (1) it clearly appears from specific facts shown by affidavit or by a verified complaint that immediate and irreparable injury, loss, or damage will result to the plaintiff before the adverse party or his attorney can be heard in opposition, and (2) the plaintiff's attorney certifies to the court in writing the efforts, if any, which have been made to give the notice and the reasons supporting his claim that notice should not be required. The party obtaining relief under this subdivision shall give written or oral notice thereof as soon as possible to the trustee, receiver, or debtor in possession and to the debtor and, in any event, shall forthwith mail to such person or persons a copy of the order granting relief. On 2 days' notice to the party

who obtained relief from a stay provided by this rule without notice or on such shorter notice to that party as the court may prescribe, the adverse party may appear and move its reinstatement, and in that event the court shall proceed to hear and determine such motion as expeditiously as the ends of justice require."

2. Rules of Bankruptcy Procedure, Rule 12-36:

"(a) *Filing of Plan by Debtor.* The debtor may file a plan with his petition or thereafter, but not later than a time fixed by the court.

"(b) *Filing of Plan by Creditors.* Within such time as may be fixed by the court, a plan may be filed by a creditor holding a security interest in real property or a chattel real dealt with by such plan.

"(c) *Number of Copies.* If required by the court, the person filing a plan shall promptly furnish a sufficient number of copies to enable the court to transmit them as provided in subdivision (d) of this rule.

"(d) *Transmittal of Plan; Adjourned Meetings.* If a plan is filed prior to mailing of notice of the first meeting of creditors, a copy of the plan shall accompany the notice. If the debtor has not filed a plan prior to the first date set for the first meeting of creditors, the court, at the first meeting or thereafter, shall fix a time for filing a plan. If the debtor has not filed a plan prior to the mailing of notice of the first meeting of creditors, the court at the first meeting, shall adjourn the meeting to a date certain. When a plan is timely filed by the debtor or a creditor, a copy thereof and notice of a subsequent adjourned meeting date shall be mailed to the persons specified in Rule 12-23(a) at least 10 days prior to such date. The court may adjourn a first meeting of creditors from time to time to dates certain."

3. **Rules of Bankruptcy Procedure, Rule 12-17(b):**

"Retention of Debtor in Possession; Appointment of Trustee. On the filing of a petition under Rule 12-6 or 12-7, if no trustee in bankruptcy has previously qualified, the debtor shall continue in possession. On application of any party in interest, the court may, for cause shown, appoint a trustee."

APPENDIX B

SECURITY DEED NOTE

$828,000 June 19, 1973

FOR VALUE RECEIVED, the undersigned, PINEGATE ASSOCIATES, LTD., (hereinafter referred to as "Pinegate"), a Georgia limited partnership, by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of said limited partnership, with a present office address: % Richard G. Holloway, 1500 Candler Building, Atlanta, Georgia 30303, promises to pay to GREAT NATIONAL LIFE INSURANCE COMPANY, (hereinafter referred to as "Great National"), a Texas corporation, having its principal place of business at Harry Hines Boulevard at Mockingbird Lane, Post Office Box 35844, Dallas, Texas 75235 or order, at the office of USLIFE Mortgage Corporation, Post Office Box 35266, Dallas, Texas 75235, or at such other place as may be designated in writing by the holder of this Note, the principal sum of EIGHT HUNDRED TWENTY EIGHT THOUSAND AND 00/100THS ($828,000.00) DOLLARS, or so much thereof as may be advanced hereunder, but in no event more than $828,000.00, with interest thereon from date, at the rate of NINE (9%) per centum per annum, such principal and interest to be paid in installments as follows:

I. In the event that on the date first above written, Great National makes an advance in the REDUCED AMOUNT OF SEVEN HUNDRED FIVE THOUSAND AND 00/100THS ($705,000.00) DOLLARS, then such principal and interest shall be paid in installments as follows:

Interest at the rate of Nine (9%) per centum per annum shall accrue from the date hereof and be paid on the first day of July, 1973 and thereafter on the first day of each of the next succeeding five months.

Thereafter, commencing on the first day of January, 1974, installments of principal and interest shall be paid in the sum of Five Thousand Eight Hundred Fifty Seven And 38/100ths ($5,857.38) Dollars each, such payments to continue monthly thereafter on the first day of each succeeding month until the entire principal and interest have been paid. In any event, the balance (if any) remaining unpaid, plus accrued interest, shall be due and payable on the first day of December, 1988. The installments of principal and interest shall be applied first to interest at the rate of Nine (9%) per centum per annum upon the principal or so much thereof as shall from time to time remain unpaid, and the balance thereof shall be applied on account of principal.

II. If, in addition to the reduced amount of Seven Hundred Five Thousand And 00/100ths ($705,000.00) Dollars advanced above, Great National shall also advance prior to December 31, 1973 an ADDITIONAL SUM OF ONE HUNDRED TWENTY THREE THOUSAND AND 00/100THS ($123,000.00) DOLLARS, then such principal and interest shall not be paid as in I above, but instead in installments as follows:

Interest at the rate of Nine (9%) per centum per annum shall accrue from the date hereof and be paid on the first day of July, 1973 and thereafter on the first day of each succeeding month either for five (5) months or until the said additional sum referred to above is advanced, whichever occurs first.

Thereafter, commencing on the first day of January, 1974 or the first day of the month following advance of the additional sum referred to above, whichever occurs first, installments of principal and interest shall be paid in the sum of Six Thousand Eight Hundred Seventy Nine And 30/100ths ($6,879.30) Dollars each, such payments to continue monthly thereafter on the first day of each succeeding month until the entire principal and interest have been paid. In any event, the balance (if any) remaining unpaid, plus accrued interest, shall be due and payable on the first day of December, 1988. The installments of principal and interest shall be applied first to interest at the rate of Nine (9%) percent per annum upon the principal or so much thereof as shall from time to time remain unpaid, and the balance thereof shall be applied on account of principal.

In the event that any payment provided for hereinabove shall become overdue for a period in excess of fifteen (15) days a late charge of four cents (4¢) for each dollar ($1.00) so overdue may be charged by the holder of this Note for the purpose of defraying the expense incident to handling such delinquent payment. Such late charge shall be deemed to be fully secured by the Security Deed securing this Note.

In addition to the payments on account of principal set forth above, the privilege is reserved to prepay the indebtedness, in full or in part, on any installment payment date commencing on the first day of the eleventh (11th) loan year, upon thirty (30) days prior written notice, in an amount equal to the principal portion of any consecutive number of regular monthly payments, and upon payment of a premium on the amount so prepaid of five (5%) percent during the eleventh (11th) loan year such premium reducing one-half (½%) percent in each succeeding loan year.

Any such additional payments on account of principal shall advance the final maturity, but shall not affect, prior to final maturity, the amount or payment date of any regular installment hereunder.

Time being of the essence hereunder, in the event any installment is not paid promptly within 5 days after the due date thereof or in the event the undersigned defaults in the performance of any of the terms, covenants or warranties contained in the Security Deed securing payment hereof, at the option of the holder of this Note, the entire unpaid principal sum evidenced hereby and secured by said Security Deed, together with all interest accrued thereon, shall immediately become due and payable without notice. No failure of the holder hereof to insist upon a strict compliance by the undersigned with his obligations hereunder or to exercise the option of accelerating the maturity of the entire indebtedness, nor any indulgence granted from time to time, nor any custom or practice on the part of the undersigned or of the holder hereof at variance with the terms hereof shall constitute a waiver of the right of the holder hereof to demand exact compliance with the terms hereof without notice to the undersigned or constitute waiver of the right of acceleration herein set forth.

Interest at the rate of twelve (12%) percent per annum shall be paid on unpaid installments after the due date thereof and on the unpaid balance of this Note after maturity, whether by acceleration or otherwise.

If this promissory Note or any installment hereof is collected by or through an attorney at law, the undersigned shall pay all costs of collection including attorney's fees in an amount equal to ten (10%) percent of the principal and interest.

The makers and endorsers hereof and all others who may become liable for all or any part of this obligation, agree hereby to be jointly and severally bound, and jointly and severally waive and renounce, each for himself and family, any and all homestead and exemption rights as well as the benefit of all valuation and appraisement privileges, under or by virtue of the constitution and laws of the State of Georgia, of any other state or of the United States, as against this debt or any renewal or extension thereof, waive presentment, demand, protest, notice of demand, notice of dishonor, notice of non-payment and any and all lack of diligence or delays in collection or enforcement hereof, and expressly consent to any extension of time, release of any party liable for this obligation, release of any of the security of this Note, acceptance of other security therefor, or any other indulgence or forbearance whatsoever. Any such extension, release, indulgence or forbearance may be made without notice to said party and without in any way affecting the personal liability of such party.

This Note and a companion note of even date in the amount of Five Hundred Fifty Two Thousand and 00/100ths ($552,000.00) Dollars executed by the undersigned and payable to the order of North American Life Insurance Company Of Chicago together represent a total indebtedness of One Million Three Hundred Eighty Thousand and 00/100ths ($1,380,000.00) Dollars and are secured by a first Security Deed of even date herewith made by and in favor of like parties conveying title to real property situate in Land Lots 241, 242, and 225 in the 6th District, County of Gwinnett, State of Georgia and are to be construed according to the laws of that State.

This Note is executed on behalf of Pinegate by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of the said limited partnership and is payable only out of the property specifically described in said Security Deed securing the payment hereof, by enforcement of the provisions contained herein and in said Security Deed. No personal liability shall be asserted or be enforceable against the Grantor or any of its individual partners, or their heirs, successors and assigns, or any person interested beneficially or otherwise in said property specifically described in said Security Deed given to secure the payment hereof, because or in respect of this Note or the making, issue or transfer thereof, all such liability, if any, is being expressly waived by each taker and holder hereof, and that so far as the Grantor and its successors and assigns and its individual partners and their heirs, successors and assigns personally are concerned, the holder hereof shall look solely to the premises conveyed by said Security Deed for the payment hereof, in the manner set forth therein and herein, provided, however, that this shall not be construed in any way so as to affect or impair the lien of said Security Deed or the Grantee's right to the foreclosure thereof by judgment against the Grantor or otherwise as provided by law, except that no judgment for any deficiency shall be demanded of the Grantor or any of its individual partners, or their heirs, successors and assigns, nor shall this be construed in any way so as to limit or restrict any of the rights and remedies of the Grantee in any foreclosure

proceeding or other enforcement of the payment of the indebtedness evidenced hereby out of and from the security given therefor, including, but without limitation, the Grantee's rights to the appointment of a receiver.

IN WITNESS WHEREOF, this Security Deed Note has been duly signed and delivered by the undersigned limited partnership by its duly authorized general partner the day and year first above written.

PINEGATE ASSOCIATES, LTD.,
a limited partnership

By: /s/ DAVID ROSS VAUGHAN
David Ross Vaughan,
Not individually but as General Partner

Signed, sealed and delivered
in the presence of:

_____

_____
Notary Public

SECURITY DEED NOTE

$552,000 June 19, 1973

FOR VALUE RECEIVED, the undersigned, PINEGATE ASSOCIATES, LTD.,(hereinafter referred to as "Pinegate"), a Georgia limited partnership, by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of said limited partnership, with a present office address: % Richard G. Holloway, 1500 Candler Building, Atlanta, Georgia 30303 promises to pay to NORTH AMERICAN LIFE INSURANCE COMPANY OF CHICAGO, (hereinafter referred to as "North American"), an Illinois corporation, having its principal place of business at 35 East Wacker Drive, Chicago, Illinois 60601, or order, at the office of USLIFE Mortgage Corporation, Post Office Box 35266, Dallas, Texas 75235, or at such other place as may be designated in writing by the holder of this Note, the principal sum of FIVE HUNDRED FIFTY-TWO AND 00/100THS ($552,000.00) DOLLARS, or so much thereof as may be advanced hereunder, but in no event more than $552,000.00, with interest thereon from date, at the rate of NINE (9%) per centum per annum, such principal and interest to be paid in installments as follows:

I. In the event that on the date first above written, North American makes an advance in the REDUCED AMOUNT OF FOUR HUNDRED SEVENTY THOUSAND AND 00/100THS ($470,000.00) DOLLARS, then such principal and interest shall be paid in installments as follows:

Interest at the rate of Nine (9%) per centum per annum shall accrue from the date hereof and be paid on the first day of July, 1973 and thereafter on the first day of each of the next succeeding five months.

Thereafter, commencing on the first day of January, 1974, installments of principal and interest shall be paid in the sum of Three Thousand Nine Hundred Four and 92/100ths ($3,904.92) Dollars each, such payments to continue monthly thereafter on the first day of each succeeding month until the entire principal and interest have been paid. In any event, the balance (if any) remaining unpaid, plus accrued interest, shall be due and payable on the first day of December, 1988. The installments of principal and interest shall be applied first to interest at the rate of Nine (9%) per centum per annum upon the principal or so much thereof as shall from time to time remain unpaid, and the balance thereof shall be applied on account of principal.

II. If, in addition to the reduced amount of Four Hundred Seventy Thousand And 00/100ths ($470,000.00) Dollars advanced above, North American shall also advance prior to December 31, 1973 an ADDITIONAL SUM OF EIGHTY TWO THOUSAND AND 00/100THS ($82,000.00) DOLLARS, then such principal and interest shall not be paid as in I above, but instead in installments as follows:

Interest at the rate of Nine (9%) per centum per annum shall accrue from the date hereof and be paid on the first day of July, 1973 and thereafter on the first day of each succeeding month either for five (5) months or until the said additional sum referred to above is advanced, whichever occurs first.

Thereafter, commencing on the first day of January, 1974 or the first day of the month following advance of the additional sum referred to above, whichever occurs first, installments of principal and interest shall be paid in the sum of Four Thousand Five Hundred Eighty Six And 20/100ths ($4,586.20) Dollars each, such payments to continue monthly thereafter on the first day of each succeeding month until the entire principal and interest have been paid. In any event, the balance (if any) remaining unpaid, plus accrued interest, shall be due and payable on the first day of December, 1988. The installments of principal and interest shall be applied first to interest at the rate of Nine (9%) per centum per annum upon the principal or so much thereof as shall from time to time remain unpaid, and the balance thereof shall be applied on account of principal.

In the event that any payment provided for hereinabove shall become overdue for a period in excess of fifteen (15) days, a late charge of four cents (4¢) for each dollar ($1.00) so overdue may be charged by the holder of this Note for the purpose of defraying the expense incident to handling such delinquent payment. Such late charge shall be deemed to be fully secured by the Security Deed securing this Note.

In addition to the payments on account of principal set forth above, the privilege is reserved to prepay the indebtedness, in full or in part, on any installment payment date commencing on the first day of the eleventh (11th) loan year, upon thirty (30) days prior written notice, in an amount equal to the principal portion of any consecutive number of regular monthly payments, and upon payment of a premium on the amount so prepaid of five (5%) percent during the eleventh (11th) loan year such premium reducing one-half (½%) percent in each succeeding loan year.

Any such additional payments on account of principal shall advance the final maturity, but shall not affect, prior to final maturity, the amount or payment date of any regular installment hereunder.

Time being of the essence hereunder, in the event any installment is not paid promptly within 5 days after the due date thereof or in the event the undersigned defaults in the performance of any of the terms, covenants, conditions or warranties contained in the Security Deed securing payment hereof, at the option of the holder of this Note, the entire unpaid principal sum evidenced hereby and secured by said Security Deed, together with all interest accrued thereon, shall immediately become due and payable without notice. No failure of the holder hereof to insist upon a strict compliance by the undersigned with his obligations hereunder or to exercise the option of accelerating the maturity of the entire indebtedness, nor any indulgence granted from time to time, nor any custom or practice on the part of the undersigned or of the holder hereof at variance with the terms hereof shall constitute a waiver of the right of the holder hereof to demand exact compliance with the terms hereof without notice to the undersigned or constitute waiver of the right of acceleration herein set forth.

Interest at the rate of twelve (12%) percent per annum shall be paid on unpaid installments after the due date thereof and on the unpaid balance of this Note after maturity, whether by acceleration or otherwise.

If this promissory Note or any installment hereof is collected by or through an attorney at law, the undersigned shall pay all costs of collection including attorney's fees in an amount equal to ten (10%) percent of the principal and interest.

The makers and endorsers hereof and all others who may become liable for all or any part of this obligation, agree hereby to be jointly and severally bound, and jointly and severally waive and renounce, each for himself and family, any and all homestead and exemption rights as well as the benefit of all valuation and appraisement privileges, under or by virtue of the constitution and laws of the State of Georgia, of any other state or of the United States, as against this debt or any renewal or extension thereof, waive presentment, demand, protest, notice of demand, notice of dishonor, notice of non-payment and any and all lack of diligence or delays in collection or enforcement hereof, and expressly consent to any extension of time, release of any party liable for this obligation, release of any of the security of this Note, acceptance of other security therefor, or any other indulgence or forbearance whatsoever. Any such extension, release, indulgence or forbearance may be made without notice to said party and without in any way affecting the personal liability of such party.

This Note and a companion note of even date in the amount of Eight Hundred Twenty Eight Thousand and 00/100ths ($828,000.00) Dollars executed by the undersigned and payable to the order of Great National Life Insurance Company together represent a total indebtedness of One Million Three Hundred Eighty Thousand and 00/100ths ($1,380,000.00) Dollars and are secured by a first Security Deed of even date herewith made by and in favor of like parties conveying title to real property situate in Land Lots 241, 242, and 225 in the 6th District, County of Gwinnett, State of Georgia and are to be construed according to the laws of that State.

This Note is executed on behalf of Pinegate by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of the said limited partnership and is payable only out of the property specifically described in said Security Deed securing the payment hereof, by enforcement of the provisions contained herein and in said Security Deed. No personal liability shall be asserted or be enforceable against the Grantor or any of its individual partners, or their heirs, successors and assigns, or any person interested beneficially or otherwise in said property specifically described in said Security Deed given to secure the payment hereof, because or in respect of this Note or the making, issue or transfer thereof, all such liability, if any, is being expressly waived by each taker and holder hereof, and that so far as the Grantor and its successors and assigns and its individual partners and their heirs, successors and assigns personally are concerned, the holder hereof shall look solely to the premises conveyed by said Security Deed for the payment hereof, in the manner set forth therein and herein, provided, however, that this shall not be construed in any way so as to affect or impair the lien of said Security Deed or the Grantee's right to the foreclosure thereof by judgment against the Grantor or otherwise as provided by law, except that no judgment for any deficiency shall be demanded of the Grantor or any of its individual partners, or their heirs, successors and assigns, nor shall this be construed in any way so as

to limit or restrict any of the rights and remedies of the Grantee in any foreclosure proceeding or other enforcement of the payment of the indebtedness evidenced hereby out of and from the security given therefor, including, but without limitation, the Grantee's rights to the appointment of a receiver.

IN WITNESS WHEREOF, this Security Deed Note has been duly signed and delivered by the undersigned limited partnership by its duly authorized general partner the day and year first above written.

PINEGATE ASSOCIATES, LTD.,
a limited partnership

By: /s/ DAVID ROSS VAUGHAN
David Ross Vaughan,
Not individually but as General Partner

Signed, sealed and delivered
in the presence of:

_____

_____

_____
Notary Public

Notary not necessary per J. Dietz,
USL — N.Y.

APPENDIX C

SECURITY DEED
AND
SECURITY AGREEMENT

THIS INDENTURE made and entered into this 19th day of June, 1973, by and between PINE GATE ASSOCIATES, LTD., a Georgia limited partnership, by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of said limited partnership, with a present office address: % Richard G. Holloway, 1500 Candler Building, Atlanta, Georgia 30303 (hereinafter with heirs, executors, administrators, successors and assigns called 'Grantor'), and GREAT NATIONAL LIFE INSURANCE COMPANY, a Texas corporation, having its home office at Harry Hines Boulevard at Mockingbird Lane, Post Office Box 35844, Dallas, Texas 75235 and NORTH AMERICAN LIFE INSURANCE COMPANY OF CHICAGO, an Illinois corporation, having its home office at 35 East Wacker Drive, Chicago, Illinois 60601 (hereinafter with their successors and assigns collectively called 'Grantee').

WITNESSETH:

THAT for the consideration hereinafter mentioned, receipt whereof is hereby acknowledged, Grantor does hereby BARGAIN, SELL, GRANT, ASSIGN AND CONVEY unto Grantee, all that certain real estate situated and being in Land Lots 225, 241 and 242 of the 6th District, County of Gwinnett, State of Georgia, to wit:

BEGINNING at an iron pin located on the southwesterly right of way line of Beaver Ruin Road (130 foot right-of-way), said iron pin also marking the northeasterly property corner of land now or formerly owned by Beard, et al., and running thence south 10 degrees 53 minutes 00 seconds west 260.2 feet to an iron pin; running thence south 31 degrees 55 minutes west, 834.40 feet to an iron pin; running thence south 58 degrees 48 minutes west, 159.7 feet to an iron pin; running thence south 10 degrees 26 minutes east 552.30 feet to an iron pin; running thence north 73 degrees 48 minutes east, 152.50 feet to an iron pin; running thence north 24 degrees 48 minutes east 967.80 feet to an iron pin; running thence north 10 degrees 53 minutes 00 seconds east, 296.86 feet to a point; running thence north 79 degrees 07 minutes 00 seconds west, 121.33 feet to a point; running thence north 10 degrees 53 minutes 00 seconds east, 344.06 feet to a point on the southwesterly right-of-way line of Beaver Ruin Road (130 foot right-of-way); running thence along the said right-of-way line of Beaver Ruin Road north 59 degrees 00 minutes 00 seconds west, 31.96 feet to an iron pin and the Point of Beginning, as shown on surveys for Beaver Ruin Associates, Inc. dated May 8, 1973 and May 22, 1973 respectively and prepared by Milton R. Lemon, Georgia Registered Land Surveyor.

TOGETHER with all right, title and interest of Grantor, including any after-acquired title or reversion, in and to the beds of the ways, streets, avenues and alleys adjoining the said premises; and

TOGETHER with all and singular the tenements, hereditaments, easements, appurtenances, passages, waters, water courses, riparian rights, other rights, liberties and privileges thereof or in any way now or hereafter appertaining, including any

other claim at law or in equity as well as any after-acquired title, franchise or license and the reversion and reversions and remainder and remainders thereof; and

TOGETHER with all buildings and improvements of every kind and description now or hereafter erected or placed thereon, and all fixtures and articles of personal property now or hereafter owned by Grantor and attached to or contained in and used in connection with said premises, including but not limited to all apparatus, machinery, motors, elevators, fittings, radiators, gas ranges, ice boxes, mechanical refrigerators, awnings, shades, screens, office equipment and other furnishings, and all plumbing, heating, lighting, cooking, laundry, ventilating, refrigerating, incinerating, air-conditioning and sprinkler equipment and fixtures and appurtenances thereto; and all renewals or replacements thereof or articles in substitution therefor, whether or not the same are or shall be attached to said building or buildings in any manner; it being mutually agreed that all the aforesaid property owned by said Grantor and placed by it on said premises shall, so far as permitted by law, be deemed to be affixed to the realty and covered by this Security Deed; and

TOGETHER with all awards and other compensation heretofore or hereafter to be given to the present and all subsequent owners of the said premises or any taking by eminent domain, either permanent or temporary, of all or any part of the said premises or any easement or appurtenance thereof, including severance and consequential damage and change in grade of streets, which said awards and compensation are hereby assigned to Grantee, and Grantor hereby appoints Grantee its Attorney-in-Fact, coupled with an interest, and authorizes, directs and empowers such Attorney, at the option of the Attorney, on behalf of Grantor or heirs, personal representatives, successors or assigns to adjust or compromise the claim for any such award and to collect and receive the proceeds thereof, to give proper receipts and acquittances therefor and, after deducting expenses of collection, to apply the net proceeds as a credit upon any portion, as selected by Grantee, of the indebtedness secured hereby, and, if any such taking shall occur in the first five (5) years of the loan term, including also payment of the premium required under the prepayment privilege, if any, contained in the said Note, or otherwise of an amount equal to five (5%) percent of the principal so prepaid, notwithstanding the fact that the amount owing thereon may not then be due and payable or that the indebtedness is otherwise adequately secured.

TO HAVE AND TO HOLD the above described real estate and property (hereinafter called the 'premises') to the use, benefit and behoof of Grantee forever in fee simple.

AND GRANTOR COVENANTS AND WARRANTS lawful seisin of an indefeasible estate in fee simple of the said premises; that the same is free from all encumbrances and liens whatsoever; except those referred to in Paragraph 35 herein which are subordinate to the lien of the within Security Deed; that Grantor has good and legal right, power and authority to so convey the same and that Grantor and successors in interest will forever WARRANT AND DEFEND the title of said property and the lien and priority of this Security Deed against the lawful claims and demands of all persons whomsoever; and that Grantor will execute, acknowledge and deliver all and every such further assurances unto the

Grantee of the title to all and singular the premises hereby conveyed and intended so to be, or which Grantor may be or shall become hereinafter bound so to do. All such covenants and warranties shall run with the land.

THIS CONVEYANCE is to be construed under the existing laws of the State of Georgia as a DEED PASSING TITLE, and not as a mortgage; and is intended to secure the payment of a debt (and interest thereon and other indebtedness as described herein) evidenced by two promissory notes of even date herewith, the terms of which are incorporated herein by reference, made by Grantor payable to Grantee or order at its office or at such other place as may be designated in writing by the holder of said Notes (said two Notes hereinafter collectively referred to as "Note" or "promissory Note") in the combined principal sum of ONE MILLION THREE HUNDRED EIGHTY AND 00/100THS ($1,380,000.00) DOLLARS, or so much thereof as may be advanced thereunder, but in no event more than $1,380,000.00, with interest thereon from date, at the rate of NINE (9%) per centum per annum, such principal and interest to be paid in installments as follows:

I. In the event that on the date first above written, Grantee makes an advance in the REDUCED AMOUNT OF ONE MILLION ONE HUNDRED SEVENTY FIVE THOUSAND AND 00/100THS ($1,175,000.00) DOLLARS, then such principal and interest shall be paid in installments as follows:

Interest at the rate of Nine (9%) per centum per annum shall accrue from the date hereof and be paid on the first day of July, 1973 and thereafter on the first day of each of the next succeeding five months.

Thereafter, commencing on the first day of January, 1974, installments of principal and interest shall be paid in the sum of Nine Thousand Seven Hundred Sixty Two and 30/100ths ($9,762.30) Dollars each, such payments to continue monthly thereafter on the first day of each succeeding month until the entire principal and interest have been paid. In any event, the balance (if any) remaining unpaid, plus accrued interest, shall be due and payable on the first day of December, 1988. The installments of principal and interest shall be applied first to interest at the rate of Nine (9%) per centum per annum upon the principal or so much thereof as shall from time to time remain unpaid, and the balance thereof shall be applied on account of principal.

II. If, in addition to the reduced amount of One Million One Hundred Seventy Five Thousand And 00/100ths ($1,175,000.00) Dollars advanced above, Grantee shall also advance prior to December 31, 1973 an ADDITIONAL SUM OF TWO HUNDRED FIVE THOUSAND AND 00/100THS ($205,000.00) DOLLARS, then such principal and interest shall not be paid as in I above, but instead in installments as follows:

Interest at the rate of Nine (9%) per centum per annum shall accrue from the date hereof and be paid on the first day of July, 1973 and thereafter on the first day of each succeeding month either for five (5) months or until the said additional sum referred to above is advanced, whichever occurs first.

Thereafter, commencing on the first day of January, 1974 or the first day of the month following advance of the additional sum referred to above, whichever occurs first, installments of principal and interest shall be paid in the sum of Eleven Thousand Four Hundred Sixty Five And 50/100ths ($11,465.50) Dollars each, such payments to continue monthly thereafter on the first day of each succeeding month until the entire principal and interest have been paid. In any event, the balance (if any) remaining unpaid, plus accrued interest, shall be due and payable on the first day of December, 1988. The installments of principal and interest shall be applied first to interest at the rate of Nine (9%) per centum per annum upon the principal or so much thereof as shall from time to time remain unpaid, and the balance thereof shall be applied on account of principal,

with privilege of prepayment, if any, as in said promissory Note more particularly set forth. In addition to the above described indebtedness, this instrument shall and does secure: (a) any and all renewals or extensions thereof, together with any and all other debts and obligations of Grantor to Grantee which are now owing or may hereafter become owing; (b) any and all advances by Grantee or by any owner of this deed to secure debt, whether the premises are still owned by Grantor or owned by a subsequent purchaser of the premises, which advances are made to pay taxes, to pay premiums on insurance on the premises, or to repair, maintain or preserve the premises or to complete improvements on it; (c) all expenses, including, but not limited to, attorneys' fees, incident to the collection of the aforesaid indebtedness and the foreclosure of this Security Deed by action in any court or by exercise of the power of sale contained herein.

GRANTOR FURTHER COVENANTS AND AGREES:

1. To pay promptly the principal of and interest on the indebtedness evidenced by the said Note at the times and in the manner herein and in said Note provided.

2. To keep the premises free from statutory liens of every kind; to pay, before delinquency and before any penalty for non-payment attaches thereto, all taxes, assessments, water rates, sewer rentals and other governmental or municipal charges, fines or impositions which are or may be levied against the premises or any part thereof and Grantee shall have the option to require deposit with Grantee concurrently with the payment of the installments due under the Note secured hereby of a sum equal to the amount of such taxes, assessments and charges respectively next due upon the said premises (all as estimated by Grantee) divided by the number of note installments to elapse before a date not less than one month prior to the date when such taxes, assessments or charges respectively shall become delinquent and all such sums shall be held by Grantee in trust to pay same; to deliver to Grantee at least ten (10) days before delinquency, receipted bills evidencing payment therefor; to pay, in full, under protest and in the manner provided by statute, any tax, assessment, rate, rental, charge, fine or imposition aforesaid which Grantor may desire to contest; and in the event of the passage, after the date of this instrument, of any law of the State of Georgia, deducting from the value of land for the purpose of taxation, any lien thereon or changing in any way the laws for the taxation of

Security Deeds or debts secured by Security Deeds for state or local purposes, or the manner of collection of any such taxes, so as to affect this Security Deed, Grantee shall have the right, at its option, to give thirty (30) days' written notice to the Grantor requiring the payment of the debt secured hereby and thereupon said debt shall become due, payable and collectible at the expiration of said thirty (30) days, provided, however, said option and right shall be unavailing and the Note and Security Deed shall remain in effect as though said law had not been enacted, if, notwithstanding such law Grantor lawfully may pay any such tax or taxes to or for the Grantee and does in fact pay same when payable.

3. To keep the improvements, now existing or hereafter erected on the premises, insured as may be required from time to time by the Grantee against loss or damage by, or abatement of rental income resulting from fire and such other hazards, casualties and contingencies (including, but not limited to, war risk insurance, if available) in such amounts and for such periods as may be required by Grantee and will pay promptly, when due, any premiums on such insurance. All such insurance shall be carried in companies approved by Grantee and the policies and renewals thereof shall be delivered to Grantee at least ten (10) days before the expiration of the old policies and shall have attached thereto standard non-contributing mortgagee clause (in favor of and entitling the Grantee to collect any and all of the proceeds payable under all such insurance), as well as standard waiver of subrogation endorsement, all to be in form acceptable to Grantee. In the event of loss, Grantor will give immediate notice by mail to Grantee. Grantor hereby authorizes Grantee, at its option, to collect, adjust and compromise any losses under any of the insurance aforesaid and after deducting costs of collection to apply the proceeds, at its option, as follows: (1) As a credit upon the indebtedness secured hereby, and, if any such loss shall occur in the first five years of the loan term, including payment of the premium required under the prepayment privilege, if any, contained in said Note or otherwise of an amount equal to five (5%) percent of the principal so prepaid, or (2) To restoring the improvements in which event Grantee shall not be obligated to see to the proper application thereof nor shall the amount so released or used be deemed a payment on any indebtedness secured hereby, or (3) To deliver same to the owner of said property. In the event of foreclosure of this Security Deed or sale under power of sale, or other transfer of title to the property covered hereby, in extinguishment of the indebtedness secured hereby, all right, title and interest of the Grantor in and to any insurance policies then in force, shall pass to the purchaser or grantee. Grantee at its option may require an escrow account for insurance premiums.

4. To carry and maintain such liability and indemnity insurance as may be required from time to time by Grantee, in forms, amounts and with companies satisfactory to Grantee. Certificates of such insurance, premiums prepaid, shall be deposited with Grantee and shall contain provision for ten (10) days' notice to Grantee prior to any cancellation thereof.

5. That no building or other improvement on the premises shall be altered, removed or demolished, nor shall any fixtures or appliances on, in or about said buildings or improvements be severed, removed, sold or mortgaged, without the

consent of Grantee; to permit, commit or suffer no waste, impairment or deterioration of said premises or any part thereof; to keep and maintain said premises and every part thereof with buildings, fixtures, machinery and appurtenances in thorough repair and condition, to effect such repairs as Grantee may reasonably require, and from time to time to make all needful and proper replacements so that said buildings, fixtures, machinery and appurtenances will, at all times, be in good condition, fit and proper for the respective purposes for which they were originally erected or installed; to comply with all statutes, orders, requirements or decrees relating to said premises by any Federal, State or Municipal authority, to observe and comply with all conditions and requirements necessary to preserve and extend any and all rights, licenses, permits (including but not limited to zoning variances, special exceptions and non-conforming uses), privileges, franchises and concessions which are applicable to the said premises or which have been granted to or contracted for by Grantor in connection with any existing or presently contemplated use of the said premises; and to permit Grantee or its agents, at all reasonable times, to enter upon and inspect the said property.

6. That the Grantor will not voluntarily create or otherwise permit to be created or filed against the property conveyed hereby, any mortgage lien or liens inferior or superior to this Security Deed or convey the said property by other security deed inferior or superior to the within Security Deed, and further, that it will keep and maintain the same free from the claim of all persons supplying labor or materials which will enter into the construction of any and all buildings now being erected or which hereafter may be erected on said premises, notwithstanding by whom such labor or materials may have been contracted, and on the failure of the Grantor to perform these covenants, or any part thereof, thereupon the principal and all arrears of interest shall, at the option of the Grantee, become due and payable, anything contained herein to the contrary notwithstanding. Subject to the provisions of Paragraph 35 herein.

7. That if at any time the United States Government or any other governmental subdivision shall require internal revenue or other documentary stamps or any other tax hereon or on the Note secured by this Security Deed, then the said indebtedness and the accrued interest thereon shall be and become due and payable at the election of the Grantee thirty (30) days after the mailing of notice of such election to Grantor; provided, however, said election and the right to elect shall be unavailing and this Security Deed and Note shall be and remain in effect, if Grantor lawfully may pay for such stamps or tax, including interest and penalties thereon, to or for Grantee and does in fact pay, when payable for all such stamps including interest and penalties thereon.

8. To save the Grantee harmless from all costs and expenses, including reasonable attorneys' fees, and costs of a title search, continuation of abstract and preparation of survey, incurred by reason of any action, suit, proceeding, hearing, motion or application before any court or administrative body (excepting an action to foreclose or to collect the debt secured hereby), in and to which Grantee may be or become a party by reason hereof, including but not limited to condemnation, bankruptcy and administration proceedings, as well as any other of the foregoing wherein proof of claim is by law required to be filed

or in which it becomes necessary to defend or uphold the terms of and the lien created by this Security Deed, and all money paid or expended by Grantee in that regard, together with interest thereon from date of such payment at the rate of Ten percent per annum, shall be so much additional indebtedness secured hereby and shall be immediately and without notice due and payable by Grantor.

9. That Grantor will give Grantee immediate notice of the actual or threatened commencement of any proceedings under eminent domain affecting all or any part of the said premises or any easement therein or appurtenance thereof, including severance and consequential damage and change in grade of streets, and will deliver to Grantee copies of any and all papers served in connection with any such proceedings. Grantor further covenants and agrees to make, execute and deliver to Grantee, at any time or times upon request, free, clear and discharged of any encumbrances of any kind whatsoever, any and all further assignments or other instruments deemed necessary by Grantee for the purpose of validly and sufficiently assigning all awards and other compensation heretofore and hereafter to be made to Grantor (including the assignment of any award from the United States Government at any time after the allowance of the claim therefor, the ascertainment of the amount thereof and the issuance of the warrant for payment thereof) for any taking either permanent or temporary, under any such proceedings.

10. That Grantor within five (5) days upon request by mail will furnish a written statement duly acknowledged of the amount due upon this Security Deed and whether any offsets or defenses exist against the indebtedness secured hereby.

11. That the Grantor and all subsequent owners of the said premises shall keep and maintain full and correct books and records showing in detail the earnings and expenses of said premises and shall permit the holder of this Security Deed or its representatives to examine such books and records and all supporting vouchers and data at any time and from time to time on request, at its offices, hereinbefore identified, or at such other location as may be mutually agreed upon; within ten (10) days after demand therefor and, in any event, within sixty (60) days following the expiration of Grantor's first fiscal year and following the expiration of each fiscal year thereafter during the term of this Security Deed, will furnish to the holder of this Security Deed a statement showing in detail all such earnings and expenses since the last such statement, verified by the affidavit of the Grantor or then owner, or if the same be a corporation, by an affidavit of its principal executive officer; and in the event that the owner shall refuse or fail to furnish any statement as aforedescribed, or in the event such statement shall be inaccurate or false, or in the event of the failure of the Grantor or any subsequent owner to permit the holder of this Security Deed or its representative to inspect the said premises or the said books and records on request, Grantee may consider such acts of the Grantor as a default hereunder and proceed in accordance with the rights and remedies afforded it under the provisions of this instrument.

12. That upon default by Grantor in performance of any of the terms, covenants or conditions herein or in said Note contained, Grantee may, at its

option and whether electing to declare the whole indebtedness due and payable or not, perform the same without waiver of any other remedy, and any amount paid or advanced by Grantee in connection therewith, or any other costs, charges or expenses incurred in the protection of said premises and the maintenance of this lien with interest thereon at the rate of twelve percent per annum shall be re-payable by the Grantor upon demand, shall be a lien upon the said premises prior to any right, title to, interest in or claim thereon attaching or accruing subsequent to the lien of this Security Deed and shall be secured by this Security Deed.

13. That Grantee, in making any payment herein and hereby authorized, in the place and stead of the Grantor, relating to taxes, assessments, water rates, sewer rentals and other governmental or municipal charges, fines, impositions or liens asserted against the premises may do so according to any bill, statement or estimate procured from the appropriate public office without inquiry into the accuracy of the bill, statement or estimate or into the validity of any tax, assessment, sale, forfeiture, tax lien or title or claim thereof; or relating to any apparent or threatened adverse title, lien, statement of lien, encumbrance, claim or charge shall be the sole judge of the legality or validity of same; or relating to the expense of repairs or replacement of any buildings, improvements, fixtures, merchandise or appurtenances upon the premises shall be the sole judge of the state of repairs and the necessity for incurring the expense of any repairs or replacement; or otherwise relating to any other purpose herein and hereby authorized, but not enumerated in this paragraph, may do so whenever, in its judgment and discretion, such advance or advances shall seem necessary or desirable to protect the full security intended to be created by this instrument, and provided further that in connection with any such advance, Grantee, at its option, may and is hereby authorized to obtain a continuation report of title prepared by a title insurance company, the cost and expenses of which shall be re-payable by the Grantor without demand and shall be secured hereby.

14. That upon default in the payment of any installment of principal and interest, or either, for 5 days under the said Note or in any of the payments required to be made hereunder, or upon default in the performance or observance of any of the terms, covenants, conditions or warranties herein contained, or should any proceeding under bankruptcy laws be brought by or against Grantor, or should a receiver be appointed for any properties of Grantor by any court in a proceeding wherein Grantor is charged with fraud or alleged to be insolvent or unable to pay its debts as they mature, then in any such event, at the option of Grantee, all sums secured hereby, shall, without notice, become immediately due and payable and the right of action thereon shall at once exist. In the event of any such default and upon acceleration of the entire indebtedness aforesaid, interest thereon shall accrue thereafter at the rate of twelve percent per annum, and if any suit or action is instituted to collect the said indebtedness or any part thereof or if it is placed in the hands of an attorney for collection, Grantor agrees to pay, in addition to the costs and expenses thereof, attorney's fees in an amount equal to Ten percent of the said principal and interest, all of which interest, costs, expenses and fees shall be

added to the amount of the debt secured hereby and covered by the security of this Deed. Time is of the essence in this contract.

15. That upon default by Grantor in the performance of any of the terms, covenants, conditions or warranties herein or in the said Note contained* Grantee, at its option, may foreclose this instrument in any court of competent jurisdiction, and shall be entitled to the immediate appointment of a receiver for the collection of the rents of said premises during the pendency of such foreclosure without alleging or proving insolvency of the Grantor, regardless of whether Grantee has an adequate remedy at law and without consideration of the value of the premises hereby conveyed as security, or any other ground usually incident to the appointment of receivers other than default in the Security Deed or the Note which it secures.

16. That upon default in the payment of any installment of principal and interest or either when due under the said Note or in any of the payments required to be made hereunder, or upon default in the performance or observance of any of the terms, covenants, conditions or warranties herein contained, then in any such event, at the option of the Grantee, Grantee may enter upon said premises, take possession and collect the rents and profits thereof; and may, with or without taking possession, sell the said premises as a whole, or any parcel thereof separately, at public sale or sales, before the Court House door in the County in which the premises or any part thereof is situated, to the highest bidder for cash, first giving notice of the time, place and terms of such sale or sales by advertising once a week for four weeks in the paper in which the Sheriff of the County wherein said land, or any part thereof, lies, publishes his advertisements. This power shall not be exhausted until said indebtedness has been satisfied, and one or more sales may be held hereunder. The Grantee may bid and purchase at any sale; and may execute and deliver to the purchaser or purchasers at any sale a sufficient conveyance of said properties sold in fee simple or such other estate, if any, as stated hereinbefore, with full warranties of title. The Grantor hereby constitutes and appoints the Grantee, or any agent or attorney of the Grantee, the agent and attorney in fact of Grantor to make such sale and conveyance, which conveyance shall be effectual to bar all equity of redemption, homestead, dower and all other exemptions of Grantor (all of which are hereby expressly waived) and shall thereby divest the Grantor of all right, title or equity that Grantor may have in and to said property and shall vest the same in the purchaser or purchasers at such sale or sales. All of the acts and doings of said attorney in fact are hereby ratified and confirmed, and any recitals in said conveyance as to the facts essential to a valid sale shall be binding upon Grantor.

17. That the proceeds of any such sale aforesaid shall be applied as follows: (1) To pay the costs and expenses of said sale, the expenses of protecting the property and an attorney's fee of Ten percent upon the amount of the sale; (2) To pay the indebtedness hereby secured; and (3) To pay the surplus, if any, to the person or persons legally entitled thereto.

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* (Which default shall continue beyond any period provided for herein.)

18. That the power and agency hereinbefore granted are coupled with an interest and are irrevocable by death or otherwise and are granted as cumulative to the remedies for collection of said indebtedness as provided by law.

19. That in the event of a sale under power as hereinabove provided, the Grantor shall then become and be a tenant holding over and shall forthwith deliver possession to the purchaser at such sale, or be summarily dispossessed, in accordance with the provisions of law applicable to tenant's holding over.

20. That the failure of the Grantee to exercise the option for acceleration of maturity or foreclosure or sale under power of sale following any default as aforesaid or to exercise any other option granted to the Grantee hereunder in any one or more instances, or the acceptance by Grantee of partial payments, hereunder shall not constitute a waiver of any such default, but such option shall remain continuously in force. Acceleration of maturity, once claimed hereunder by Grantee, may, at the option of Grantee, be rescinded by written acknowledgement to that effect by Grantee, but the tender and acceptance of partial payments alone shall not in any way affect or rescind such acceleration of maturity.

21. That all right, title and interest of the Grantor in and to all leases affecting the said premises together with any and all further leases upon all or any part of the said premises, and together with all of the rents, income, receipts, revenues, issues and profits from or due or arising out of the said premises have been transferred and assigned simultaneously herewith to Grantee as further security for the payment of the said indebtedness under provisions of a certain Assignment of Lessor's Interest in Lease(s) of even date herewith executed by Grantor and to be recorded simultaneously herewith, the terms, covenants and conditions of which are hereby expressly incorporated herein by reference and made a part hereof, with the same force and effect as though the same were more particularly set forth herein.

22. That at the option of Grantee this Security Deed shall become subject and subordinate, in whole or in part (but not in respect to the priority of entitlement to insurance proceeds or any award in condemnation) to any and all leases, of all or any part of the said premises, upon the execution by Grantee and recording thereof, at any time hereafter, in the Office of the Clerk of the Superior Court, in and for the county wherein the said premises are situate, of a unilateral declaration to that effect.

23. That should the proceeds of the loan made by the Grantee to the Grantor, the re-payment of which is hereby secured, or any part thereof, or any amount paid out or advanced by the Grantee, be used directly or indirectly to pay off, discharge or satisfy, in whole or in part, any prior lien or encumbrance upon said premises abovedescribed, or any part thereof, then the Grantee shall be subrogated to any additional security held by the holder of such lien or encumbrance.

24. That the rights and remedies herein provided are cumulative and that the Grantee, as holder of said Note and every other obligation secured hereby, may recover judgment thereon, issue execution therefor and resort to every other

right or remedy available at law or in equity, without first exhausting and without affecting or impairing the security or any right or remedy afforded by this Security Deed, and no enumeration of special rights or powers by any provision of this Security Deed shall be construed to limit any grant of general rights or powers, or to take away or limit any and all rights granted to or vested in the Grantee by virtue of the laws of Georgia.

25. That Grantee, without notice and without regard to the consideration, if any, paid therefor, and notwithstanding the existence at that time of any inferior liens thereon, may release any part of the security described herein or may release any person liable for any indebtedness secured hereby without in any way affecting the priority of the lien of this Security Deed, to the full extent of the indebtedness remaining unpaid hereunder, upon any part of the security not expressly released. The Grantee may also agree with any party obligated on said indebtedness or having any interest in the security described herein to extend the time for payment of any part or all of the indebtedness secured hereby, and such agreement shall not, in any way, release or impair the lien hereof, but shall extend the lien hereof as against the title of all parties having any interest in said security, which interest is subject to said lien.

26. In the event the Grantee (a) releases, as aforesaid, any part of the security described herein or any person liable for any indebtedness secured hereby, or (b) grants an extension of time on any payments of the indebtedness secured hereby, or (c) takes other or additional security for the payment thereof, or (d) waives or fails to exercise any right granted herein or in said promissory Note, said act or omission shall not release the Grantor, subsequent purchasers of the said premises or any part thereof, or makers or sureties of this Security Deed or of said promissory Note, under any covenant of this Security Deed or of the said promissory Note, nor preclude the Grantee from exercising any right, power or privilege herein granted or intended to be granted in the event of any other default then made or any subsequent default.

27. To give immediate notice by mail to the Grantee of any conveyance, transfer or change of ownership of the premises.

28. That nothing herein contained nor any transaction related thereto shall be construed or so operate as to require the Grantor to pay interest at a rate greater than it is now lawful in such case to contract for, or to make any payment or to do any act contrary to law; that if any clauses or provisions herein contained operate or would prospectively operate to invalidate this Security Deed in whole or in part, then such clauses and provisions only shall be held for naught, as though not herein contained, and the remainder of this Security Deed shall remain operative and in full force and effect.

29. That to the extent permitted by law with respect to the debt secured hereby or any renewals or extensions thereof, Grantor jointly and severally waives and renounces, each for himself and family, any and all homestead and exemption rights, as well as the benefit of all valuation and appraisement privileges under or by virtue of the constitution and laws of the State of Georgia, of any other state or of the United States now existing or hereafter enacted.

30. That, if the Grantor or any subsequent owner is a corporation, to preserve, maintain and keep in full force and effect its corporate existence, its right to carry on its business and all franchises, rights or privileges heretofore or hereafter granted to or conferred upon Grantor.

31. This Security Deed shall constitute a Security Agreement under the Georgia Uniform Commercial Code as to all fixtures, personal property and other property of any kind to which the said Uniform Commercial Code now or hereafter applies to the end that the Grantee shall have and may enforce a security interest in such fixtures, personal property and other property in addition to any and all other liens and rights granted or created under the provisions hereof or under other applicable law. The Grantor hereby authorizes the Grantee to file, without the signature of the Grantor, such financing statement or statements as may be required in the opinion of the Grantee to perfect, preserve and maintain the security interests provided for herein.

32. Should Grantor deed, quitclaim, assign, convey, transfer, sell, sell under contract of sale, lease with option to purchase, dispose of or further encumber said property, or any part thereof, or any interest therein, or agree to do so, or such shall occur by any means, voluntary or involuntary, by operation of law or otherwise, then all sums due and owing to the Grantee under this Security Deed shall immediately become due and owing unless the Grantee shall have consented thereto in writing. Failure to pay such sums shall constitute a default hereunder. Consent to one such transaction shall not be deemed to be a waiver of the right to require such consent to future or successive transactions.

33. Upon any default and following the acceleration of maturity as aforesaid, a tender of payment of the amount necessary to satisfy the entire indebtedness secured hereby, made at any time prior to foreclosure sale by the Grantor or by anyone in behalf of the Grantor shall constitute an evasion of the prepayment privilege and shall be deemed to be a voluntary prepayment hereunder and such payment, to the extent permitted by law, will therefore include the premium required under the prepayment privilege, if any, contained in the Note secured hereby, or if at that time there be no such prepayment privilege, then such payment to the extent permitted by law, will include a premium for such prepayment of five (5%) percent of the then principal balance.

34. Reference is here made to a certain Declaration Of Restrictions of even date herewith executed by Grantor, which is to be recorded in the official records of Gwinnett County, Georgia prior to the recording of the within Security Deed. The said Declaration Of Restrictions affects the use of a nine-tenths (.9) acre parcel, more particularly described therein and contiguous to the secured premises described herein on page 1, which is to be conveyed, subject to the said Declaration Of Restrictions, by Grantor herein to David Ross Vaughan, an individual, by a Warranty Deed of even date herewith which also is to be recorded in the aforesaid official records of Gwinnett County, Georgia prior to the recording of the within Security Deed. Grantor acknowledges that it executed the aforesaid Declaration Of Restrictions and made its conveyance of the aforesaid contiguous parcel subject to the said Declaration Of Restrictions

at the request of and for the benefit of the Grantee herein, its successors and assigns. Any violation of or non-compliance with the said Declaration Of Restrictions without the prior written consent of the Grantee shall constitute a default hereunder and all sums due and owing to the Grantee under this Security Deed, at the sole option of the Grantee, shall become due and owing. However, if the remedy of an injunction is available and the Grantor herein is proceeding diligently to commence and prosecute an action or suit to enjoin said violation or non-compliance, the Grantee will not avail itself of its rights hereunder pending the outcome of the said action or suit. Failure on the part of the Grantee to declare all sums immediately due and owing or to avail itself of its rights hereunder for any one such violation or non-compliance of the said Declaration Of Restrictions shall not be deemed to be a waiver of the right to declare such sums immediately due and owing for any future violation or non-compliance thereof.

35. It is understood by Grantee that there is presently a Deed to Secure Debt encumbering the property described on Page 1 hereof in favor of First American Investment Corporation and Fidelity Capital Corporation, recorded in Deed Book 444, page 45, Gwinnett County records, which Deed to Secure Debt has been subordinated to the lien hereof by a certain Subordination Agreement of even date herewith between the Grantee herein and the said First American Investment Corporation and Fidelity Capital Corporation. Grantor and Grantee hereby agree that any default under the terms of the Deed to Secure Debt recorded in Deed Book 444, page 45, Gwinnett County records, above referred to, or under the terms of the Note secured thereby, may at the option of the Grantee herein be declared and deemed to be a default under the terms of the within instrument.

It is also understood by Grantee that the Grantor shall, after executing the within Security Deed, execute a Second Deed to Secure Debt encumbering the property described on Page 1 hereof in favor of First American Investment Corporation and Fidelity Capital Corporation, which Second Deed to Secure Debt shall, by its express terms, be subject and subordinate to the lien of the within Security Deed and is to be recorded in the official records of Gwinnett County, Georgia after the within instrument. Grantee will give First American Investment Corporation and Fidelity Capital Corporation written notice of any default which occurs prior to December 31, 1973 under the within Security Deed together with a period of fifteen (15) days following receipt of such notice during which period First American Investment Corporation and Fidelity Capital Corporation shall have the right, but not the obligation, to cure any such default. Grantor and Grantee hereby agree that any default under the terms of the said Second Deed to Secure Debt, above referred to, or under the terms of the Note secured thereby, may at the option of the Grantee herein be declared and deemed to be a default under the terms of the within instrument.

36. Any notices required or permitted to be given hereunder by the Grantor to the Grantee shall be given by Registered or Certified Mail addressed as follows unless the parties may designate in writing another address for the purpose of receiving notices hereunder:

Great National Life Insurance Company
and
North American Life Insurance Company of Chicago
% USLIFE Mortgage Corporation
Post Office Box 35266
Dallas, Texas 75235

37. That the mailing of a written notice or demand addressed to the owner of record of the said premises, or directed to the said owner at the last address actually furnished to the Grantee, or directed to said owner at said premises, and mailed by the United States mails, shall be sufficient notice and demand in any case arising under this instrument and required by the provisions hereof or by law.

38. That all the covenants and warranties herein shall run with the land.

39. This Security Deed is executed on behalf of Grantor by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of the said limited partnership and it is expressly understood and agreed that nothing contained herein or in the two Notes which this instrument secures shall be construed as creating any personal liability against the Grantor or any of its individual partners, or their heirs, successors and assigns, or any person interested beneficially or otherwise in the premises hereby conveyed personally to pay the said Notes or any interest that may accrue thereon, or any indebtedness accruing hereunder, all such liability, if any, being expressly waived by the Grantee and by every person now or hereafter claiming any right or security hereunder, and that so far as the Grantor and its successors and assigns and its individual partners and their heirs, successors and assigns personally are concerned, the legal holder or holders of said Notes and the owner or owners of any indebtedness accruing hereunder shall look solely to the premises hereby conveyed for the payment thereof in the manner set forth herein and in the said Notes; provided, however, that this shall not be construed in any way so as to affect or impair the lien of this Security Deed or the Grantee's right to the foreclosure hereof by judgment against the Grantor or otherwise as provided by law, except that no judgment for any deficiency shall be demanded of the Grantor or any of its individual partners, or their heirs, successors and assigns, nor shall this be construed in any way so as to limit or restrict any of the rights and remedies of the Grantee in any foreclosure proceeding or other enforcement of the payment of the indebtedness secured hereby out of and from the security given therefor, including, but without limitation, the Grantee's right to the appointment of a receiver.

ALL OF THE COVENANTS herein contained are joint and several and shall also bind, and the benefits and advantages thereof shall also inure to the respective heirs, executors, administrators, successors and assigns of the parties hereto. Whenever used, the singular number shall include the plural, the plural the singular and the use of any gender shall include all genders.

IN WITNESS WHEREOF, this Security Deed has been duly signed, acknowledged and delivered by the undersigned limited partnership by its duly authorized general partner the day and year first above written.

PINEGATE ASSOCIATES, LTD.,
a limited partnership

By: /s/ DAVID R. VAUGHAN
David Ross Vaughan,
Not individually but as General Partner

Signed, sealed and delivered
in the presence of:

/s/ RICHARD G. HOLLOWAY

/s/ BETTY J. McRAE

Notary Public, Georgia State at Large
My Commission Expires, Nov. 2, 1974

ACKNOWLEDGEMENT

STATE OF GEORGIA }
COUNTY OF } SS:

On this 19th day of June, 1973, before me a Notary Public in and for the State of Georgia, County of ..... personally appeared David Ross Vaughan, to me known to be the general partner of PINEGATE ASSOCIATES, LTD., the limited partnership described in and which executed the within instrument, to whom I first made known the contents thereof, and acknowledged that he signed, sealed and delivered the same on behalf of said partnership as the free and voluntary act and deed of said partnership for the uses and purposes therein mentioned.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal the day and year of this certificate above written.

BETTY J. McRAE
Notary Public

Notary Public, Georgia State at Large
My Commission Expires, Nov. 2, 1974

APPENDIX D

ASSIGNMENT OF LEASES AND RENTS

THIS ASSIGNMENT, made this 19th day of June, 1973, by PINEGATE ASSOCIATES, LTD., a Georgia limited partnership, by its general partner, David Ross Vaughan, not individually but as general partner for and on behalf of said limited partnership, with a present office address: % Richard G. Holloway, 1500 Candler Building, Atlanta, Georgia 30303 (hereinafter called "Assignor") in favor of GREAT NATIONAL LIFE INSURANCE COMPANY, a Texas corporation, having its home office at Harry Hines Boulevard at Mockingbird Lane, Post Office Box 35844, Dallas, Texas 75235 and NORTH AMERICAN LIFE INSURANCE COMPANY OF CHICAGO, an Illinois corporation, having its home office at 35 East Wacker Drive, Chicago, Illinois 60601 (hereinafter with their successors and assigns collectively called "Assignee"),

WITNESSETH:

FOR VALUE RECEIVED, Assignor does hereby SELL, ASSIGN, TRANSFER, SET OVER and DELIVER unto the Assignee all leases, written or oral, and all agreements for use or occupancy of any portion of the premises together with buildings and improvements thereon (hereinafter called "said premises"), situate in Land Lots 241, 242, 225 in the 6th District, County of Gwinnett, State of Georgia, and more particularly described in the Mortgage or Deed of Trust hereinafter identified,

TOGETHER with any and all extensions and renewals thereof and any and all further leases, lettings or agreements (including subleases thereof and tenancies following attornment) upon or covering use or occupancy of all or any part of the said premises (all such leases, agreements, subleases and tenancies heretofore mentioned are hereinafter collectively included in the designation "said leases"),

TOGETHER with any and all guarantees of lessee's performance under any of said leases, and

TOGETHER with the immediate and continuing night to collect and receive all of the rents, income, receipts, revenues, issues and profits now due or which may become due or to which Assignor may now or shall hereafter (including the period of redemption, if any) become entitled or may demand or claim, arising or issuing from or out of the said leases or from or out of the said premises or any part thereof, including but not by way of limitation: minimum rents, additional rents, percentage rents, parking maintenance, tax and insurance contributions, deficiency rents and liquidated damages following default, the premium payable by any lessee upon the exercise of a cancellation privilege originally provided in any said lease, and all proceeds payable under any policy of insurance covering loss of rents resulting from untenantability caused by destruction or damage to the said premises together with any and all rights and claims of any kind which Assignor may have against any lessee under such leases or any subtenant or occupants of the said premises (all such moneys, rights and claims in this paragraph described being hereinafter called "rents"),

SUBJECT, however, to a license hereby granted by Assignee to Assignor, but limited as hereinafter provided, to collect and receive all of the said rents.

TO HAVE AND TO HOLD the same unto the Assignee, its successors and assigns forever, or for such shorter period as hereinafter may be indicated.

FOR THE PURPOSE OF SECURING the payment of the indebtedness evidenced by two certain Notes dated of even date herewith in the combined principal sum of ONE MILLION THREE HUNDRED EIGHTY THOUSAND AND 00/100THS ($1,380,000.00) DOLLARS made by Assignor, one payable to the order of Great National Life Insurance Company and the other payable to the order of North American Life Insurance Company of Chicago, and presently held by Assignee, including any extensions and renewals thereof and any note or notes supplemental thereto, as well as the payment, observance, performance and discharge of all other obligations, covenants, conditions and warranties contained in the Mortgage or Deed of Trust to be recorded therein immediately prior in time to the recording hereof, and in any extensions, supplements and consolidations thereof, covering the said premises and securing the said Note or notes (hereinafter collectively called "the said Note and Mortgage or Deed of Trust").

TO PROTECT THE SECURITY OF THIS ASSIGNMENT, IT IS COVENANTED AND AGREED AS FOLLOWS:

1. That Assignor represents and warrants: That Assignor is the owner in fee simple absolute of the said premises and has good title to the leases and rents hereby assigned and good right to assign the same, and that no other person, firm or corporation has any right, title or interest therein; that Assignor has duly and punctually performed all and singular the terms, covenants, conditions and warranties of the existing leases on Assignor's part to be kept, observed and performed; that Assignor has not previously sold, assigned, transferred, mortgaged or pledged the said rents, from said premises, whether now due or hereafter to become due; that any of said rents due and issuing from said premises or from any part thereof for any period subsequent to the date hereof have not been collected and that payment of any of same has not otherwise been anticipated, waived, released, discounted, set off or otherwise discharged or compromised; that Assignor has not received any funds or deposits from any lessee in excess of two months' rent for which credit has not already been made on account of accrued rents; and that the lessee under any existing lease is not in default of any of the terms thereof.

2. That Assignor covenants and agrees as follows: To observe, perform and discharge, duly and punctually, all and singular the obligations, terms, covenants, conditions and warranties of the said Note and Mortgage or Deed of Trust, of the existing leases and of all future leases affecting the said premises, on the part of the Assignor to be kept, observed and performed, and to give prompt notice to Assignee of any failure on part of Assignor to observe, perform and discharge same; to notify and direct in writing each and every present or future lessee or occupant of the said premises or of any part thereof that any security deposit or other deposits heretofore delivered to Assignor have been retained by Assignor or assigned and delivered to Assignee as the case may be; to enforce or secure in the name of the Assignee the performance of each and every obligation, term, covenant, condition and agreement in said leases by any

lessee to be performed; to appear in and defend any action or proceeding arising under, occurring out of, or in any manner connected with the said leases or the obligations, duties or liabilities of the Assignor and any lessee thereunder, and, upon request by Assignee, will do so in the name and behalf of the Assignee but at the expense of the Assignor, and to pay all costs and expenses of the Assignee, including attorney's fees in a reasonable sum in any action or proceeding in which the Assignee may appear.

3. That Assignor further covenants and agrees as follows: Not to receive or collect any rents from any present or future lessee of said premises or any part thereof for a period of more than two months in advance (whether in cash or by promissory note), nor pledge, transfer, mortgage or otherwise encumber or assign future payments of said rents; not to waive, excuse, condone, discount, set off, compromise, or in any manner release or discharge any lessee thereunder, of and from any obligations, covenants, conditions and agreements by said lessee to be kept, observed and performed, including the obligation to pay the rents thereunder, in the manner and at the place and time specified therein; not to cancel, terminate or consent to any surrender of any said lease, nor modify, or in any way alter the terms thereof without, in each such instance enumerated in this paragraph, the prior written consent of the Assignee.

4. That in the event any representation or warranty herein of Assignor shall be found to be untrue or Assignor shall default in the observance or performance of any obligation, term, covenant, condition or warranty herein, then, in each such instance, the same shall constitute and be deemed to be a default under the said Note and Mortgage or Deed of Trust hereby entitling Assignee to declare all sums secured thereby and hereby immediately due and payable and to exercise any and all of the rights and remedies provided thereunder and hereunder as well as by law.

5. That so long as there shall exist no default by Assignor in the payment of any indebtedness secured hereby or in the observance and performance of any other obligation, term, covenant or condition or warranty herein or in said Note and Mortgage or Deed of Trust or in said leases contained, Assignor shall have the right under a license granted hereby (but limited as provided in the following paragraph) to collect upon, but not prior to accrual, as aforesaid all of said rents, arising from or out of the said leases or any renewals or extensions thereof, or from or out of the said premises or any part thereof, and Assignor shall receive such rents, and shall hold same, as well as the right and license to receive same, as a trust fund to be applied and Assignor hereby covenants to so apply same, first to the payment of taxes and assessments upon said premises before penalty or interest are due thereon, secondly to the cost of such insurance and of such maintenance and repairs as is required by the terms of the said Mortgage or Deed of Trust, and thirdly to the payment of interest and principal becoming due on the said Note and Mortgage or Deed of Trust, before using any part of the same for any other purposes.

6. That upon or at any time after default in the payment of any indebtedness secured hereby or in the observance or performance of any obligation, term, covenant, condition or warranty herein or in the said Note and Mortgage or

Deed of Trust or in the said leases contained, Assignee, at its option, shall have the complete right, power and authority hereunder then or thereafter to exercise and enforce any or all of the following rights and remedies: (a) to terminate the license granted to Assignor to collect as aforesaid the said rents, and then and thereafter, without taking possession, in Assignee's own name, to demand, collect, receive, sue for, attach and levy the said rents, to give proper receipts, releases and acquittances therefor, and after deducting all necessary and proper costs and expenses of collection, as determined by Assignee, including reasonable attorneys' fees, to apply the net proceeds thereof, together with any funds of Assignor deposited with Assignee, upon any indebtedness secured hereby and in such order as Assignee may determine; (b) to declare all sums secured hereby immediately due and payable and, at its option, exercise all of the rights and remedies contained in said Note and Mortgage or Deed of Trust; and (c) without regard to the adequacy of the security, with or without any action or proceeding, through any person or by agent, or by the trustee(s) under the Deed of Trust secured hereby, or by a receiver to be appointed by court and irrespective of said Assignor's possession, then or thereafter, to enter upon, take possession of, manage and operate said premises or any part thereof, make, modify, enforce, cancel or accept surrender of any lease now in effect or hereafter in effect on said premises or any part thereof; remove and evict any lessee; increase or reduce rents; decorate, clean and make repairs; and otherwise do any act or incur any costs or expense as Assignee shall deem proper to protect the security hereof, as fully and to the same extent as Assignor could do if in possession, and in such event to apply the rents so collected to the operation and management of said premises, but in such order as Assignee shall deem proper, and including payment of reasonable management, brokerage and attorney's fees, payment of the indebtedness under the said Note and Mortgage or Deed of Trust and maintenance, without interest thereon, of a reserve for replacement;

Provided, however, that the acceptance by Assignee of this Assignment, with all of the rights, powers, privileges and authority so created, shall not, prior to entry upon and taking of possession of said premises by Assignee, be deemed or construed to constitute Assignee a mortgagee in possession nor thereafter or at any time or in any event obligate the Assignee to appear in or defend any action or proceeding relating to the said leases or to the said premises, or to take any action hereunder, or to expend any money or incur any expenses or perform or discharge any obligation, duty or liability under said leases, or to assume any obligation or responsibility for any security deposits or other deposits delivered to Assignor by any lessee thereunder and not assigned and delivered to Assignee, nor shall Assignee be liable in any way for any injury or damage to person or property sustained by any person or persons, firm or corporation in or about the said premises;

And provided further that the collection of said rents and application as aforesaid and/or the entry upon and taking possession of the said premises shall not cure or waive any default or waive, modify or affect any notice of default under said Note and Mortgage or Deed of Trust to invalidate any act done pursuant to such notice, and the enforcement of such right or remedy by Assignee,

once exercised, shall continue for so long as Assignee shall elect, notwithstanding that the collection and application aforesaid of such rents may have cured for the time the original default. If Assignee shall thereafter elect to discontinue the exercise of any such right or remedy, the same or any other right or remedy hereunder may be reasserted at any time and from time following any subsequent default.

7. That Assignor hereby agrees to indemnify and hold the Assignee harmless of and from any and all liability, loss, damage or expense which it may or might incur under or by reason of this Assignment, or for any action taken by the Assignee hereunder, or by reason or in defense of any all claims and demands whatsoever which may be asserted against Assignee arising out of said leases, including, but without limitation thereto, any claim by any lessee of credit for rental paid to and received by Assignor, but not delivered to Assignee, for any period under any said lease more than two months in advance of the due date thereof; should the Assignee incur any such liability, loss, damage or expense, the amount thereof (including reasonable attorney's fees) with interest thereon at the penalty rate set forth in said Note and Mortgage or Deed of Trust shall be payable by Assignor immediately without demand, and shall be secured hereby and by said Mortgage or Deed of Trust.

8. That until the indebtedness secured hereby shall have been paid in full, Assignor will deliver to Assignee executed copies of any and all other and future leases upon all or any part of the said premises and will transfer and assign to Assignee, upon the same terms and conditions as herein contained, such other and future leases and Assignor hereby covenants and agrees to make, execute and deliver unto Assignee upon demand and at any time or times, any and all assignments and other instruments sufficient for the purpose or that the Assignee may deem to be advisable for carrying out the true purposes and intent of this Assignment (including assignment of the rent under any lease with the United States Government after allowance of the rental claim, ascertainment of the amount due and issuance of the warrant for payment thereof).

9. That the failure of the Assignee to avail itself of any of the terms, covenants and conditions of this Assignment for any period of time or at any time or times, shall not be construed or deemed to be a waiver by Assignee of any of its rights and remedies under said Note and Mortgage or Deed of Trust, or under the laws of the state in which the said premises are situate. The right of the Assignee to collect the said indebtedness and to enforce any other security therefor may be exercised by Assignee, either prior to, simultaneously with, or subsequent to any action taken hereunder.

10. That upon payment in full of all of the indebtedness secured by said Note and Mortgage or Deed of Trust and of all sums payable hereunder, this Assignment shall become and be void and of no effect, but the affidavit, certificate, letter or statement of any officer of Assignee showing any part of said indebtedness to remain unpaid shall be and constitute conclusive evidence of the validity, effectiveness and continuing force of this Assignment, and any person, firm or corporation, may and is hereby authorized to rely thereon. A demand on any lessee made by Assignee for payment of rents by reason of any

default claimed by Assignee shall be sufficient warrant to said lessee to make future payments of rents to Assignee without the necessity for further consent by the said Assignor.

11. That all notices, demands or documents of any kind which Assignee may be required or may desire to serve upon Assignor hereunder shall be sufficiently served by delivering same to Assignor personally or by leaving a copy of same addressed to Assignor at the address appearing hereinabove, or by depositing a copy of same in the United States mail, postage prepaid and addressed to Assignor at said address.

12. That the terms, covenants, conditions and warranties contained herein and the powers granted hereby shall run with the land, shall inure to the benefit of and bind all parties hereto and their respective heirs, executors, administrators, successors and assigns, and all lessees, sub-tenants and assigns of same, and all occupants and subsequent owners of the said premises, and all subsequent holders of the said Note and Mortgage or Deed of Trust. In this Assignment, whenever the context so requires, the masculine gender shall include the feminine and/or neuter and the singular number shall include the plural and conversely in each case. All obligations of each Assignor hereunder shall be joint and several.

IN WITNESS WHEREOF, this Assignment has been duly executed by the Assignor the day and year first above written.

PINEGATE ASSOCIATES, LTD.,
a limited partnership

By: DAVID ROSS VAUGHAN
David Ross Vaughan
Not individually but as General Partner

Signed, sealed and delivered
in the presence of:

RICHARD G. HOLLOWAY

BETTY J. McRAE
Notary Public

Notary Public, Georgia State at Large
My Commission Expires, Nov. 2, 1974

ACKNOWLEDGEMENT

STATE OF GEORGIA }
COUNTY OF } SS:

On this 19th day of June, 1973, before me a
Notary Public in and for the State of Georgia, County of
personally appeared David Ross Vaughan, to me known to be the general partner of PINEGATE ASSOCIATES, INC., the limited partnership described in and which executed the within instrument, to whom I first made known the contents thereof, and acknowledged that he signed, sealed and delivered the same on behallf of said partnership as the free and voluntary act and deed of said partnership for the uses and purposes therein mentioned.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal the day and year of this certificate above written.

BETTY J. McREA
Notary Public

Notary Public, Georgia State at Large
My Commission Expires, Nov. 2, 1974

APPENDIX E

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN THE MATTER OF: PINE GATE ASSOCIATES, LTD., Debtor	IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII
GREAT NATIONAL LIFE INSURANCE COMPANY, The Secured Creditor, formerly known as USLIFE LIFE INSURANCE COMPANY OF TEXAS, and ALL AMERICAN LIFE AND CASUALTY COMPANY, Plaintiffs vs. PINE GATE ASSOCIATES, LTD., Defendant	CIVIL ACTION FILE NO. B75-4345A

ORDER

This is an action by secured creditors seeking relief from the effects of an automatic stay pursuant to Rule 12-43 of the Bankruptcy Act and for interim orders to compel the Debtor to post a bond to indemnify the creditors against diminution in the value of certain property in which they have a security interest; to compel payment of rents and profits; and to authorize advertising pursuant to Georgia Law authorizing nonjudicial foreclosure of deeds to secure debt, after default, until the matter reaches a final adjudication on the merits. On January 28, 1976, plaintiffs Great National Life Insurance Company (formerly known as USLife Life Insurance Company of Texas) and All American Life and Casualty Company moved this Court for orders compelling payment of rents, issues and profits, for a bond to indemnify against loss, and for authority to advertise pursuant to Georgia Code Annotated, Section 37-607. On February 17, 1976, this Court held a hearing at which time it heard oral argument concerning each of the three foregoing motions. Having entertained the arguments of counsel and having considered each of the pending motions, the Court rules as follows:

I.

Plaintiffs have moved for an order requiring defendant Pine Gate Associates, Ltd. (hereinafter referred to as "Pine Gate") to post a bond or other sufficient security to indemnify plaintiffs against any loss or diminution of the value of their security, and any costs, losses, or damages which may be suffered by reason of the continued maintenance of the automatic stay against foreclosure pursuant to Rule 12-43 of the Bankruptcy Act. Plaintiffs argue that due to the operation of the automatic stay they are prevented from realizing upon their security to the extent that today's marketplace may allow, and that change in market conditions or unpredictable or unforeseen disaster may seriously damage their collateral before

they are able to regain possession of it. But for the automatic stay, plaintiffs contend they would be able to commence the sale of the apartment complex property pursuant to a power of sale contained in the security deed. They contend that the stay imposed herein has unconstitutionally taken their property without notice or opportunity to be heard and is, therefore, a violation of the due process clause of the Fourteenth Amendment to the United States Constitution. Plaintiffs point out that it is not only the lack of notice or hearing prior to the issuance of the injunction that makes the automatic stay against their foreclosure unconstitutional, but also the fact that property rights have been taken without just compensation.

Essentially, plaintiffs' arguments focus on two points. The first is that due to the operation of the bankruptcy rules, Pine Gate has obtained a "free" injunction in the sense that it otherwise would have had to post a bond had it filed an action to stay foreclosure in the State Court or have bargained with plaintiffs for further indulgences. Secondly, it argues that in order for its property rights to be fully protected, it is imperative that a bond be posted by the debtor in order to protect plaintiffs against diminution in the present value of the security which may occur prior to such time as the secured creditors are either fully compensated or they obtain their property pursuant to foreclosure following a final adjudication on the merits. The bond which the plaintiffs seek would assess the probability that the value of the secured property would deteriorate during the pendency of these proceedings, ultimately comparing its value at this time with its value at the date of repossession should the secured property be returned to the plaintiffs pursuant to a foreclosure sale.

Plaintiffs have presented no evidence whatsoever on the likelihood that the property which constitutes their security will diminish in value during this proceeding and they have also presented no evidence whatsoever that a bond such as they propose can be obtained. It should be emphasized that the bond sought by the plaintiffs is not the defalcation or performance bond which is sometimes considered appropriate in proceedings under the Bankruptcy Act. The bond sought by the plaintiffs is one which would protect them against diminution of the value of their security during this proceeding as a result of developments in the market. In the absence of any evidence from the plaintiffs that good reason exists for requiring such a bond, this court has no basis upon which to require it even if the plaintiffs could show that such a bond is available which they have not done.

Also, the Court finds that in this case the automatic stay pursuant to Rule 12-43 does not constitute an impermissible taking of the property rights of a creditor prior to a hearing. See *John Hancock Mutual Life Insurance Company v. Casey*, 134 F. 2d 162 (1st Cir. Ct. of App., 1943). The United States Constitution, through the Bankruptcy Act, does permit some inconvenience and encroachment upon property rights of creditors. It is only when various encroachments are lumped together as to impair the security, and become unduly burdensome on the creditor, or to impinge upon due process resulting from arbitrary and unreasonable procedures, that courts have found an unconstitutional taking of property rights. (Compare: *Louisville Joint Stock Land Bank v. Radford*, 295 US 555 (1936); and *Wright v. Vinton Branch*, 300 US 440 (1936); both written by Justice

Brandeis.[1] The petition initiating this proceeding was only filed on December 23, 1975, and the First Meeting of Creditors was held on February 10, 1976. The Debtor has been given only until March 29, 1976, to file its Plan of Arrangement with the Court. In the opinion of this Court, the automatic stay entered in this case, or the continuation thereof to this date, cannot be held to be unreasonable under these circumstances. Therefore, this Court holds that where, as here, a secured creditor has extensive, specified procedural rights to various remedies and hearings under the Bankruptcy Act (such as the instant motion for a bond, and the application for relief from the stay and the validity of the stay order), the automatic injunction does not amount to a taking of the plaintiffs' property without due process of law. Further, the Court holds that plaintiffs have failed to meet the burden of establishing that a bond should be issued, and the motion for a bond is hereby DENIED.

2.

Plaintiffs' second motion seeks to obtain an order for sequestration of rents and profits issuing from the secured property. The motion is based on Paragraph 6(a) of an agreement between the plaintiffs and the debtor entitled an "Assignment of Leases and Rents" which provides, *inter alia*, that upon default in payment of the debt, plaintiffs have the right to terminate the license granted to Pine Gate to collect rents and, thereafter, without taking possession of the property in plaintiffs' own name, demand, collect, receive, sue for and attach a levy for such rents. Plaintiffs argue that the rent money presently being collected from the tenants residing at the apartment complex referred to in the deed to secure debt is a commodity which has a value which may rise or fall with the passage of time. Plaintiffs further argue that such monies should be invested for possible profit for the benefit of its shareholders and that they are deprived of their right to do so if this Court continues to allow the debtor-in-possession to collect, hold, and spend the money. While plaintiffs agree that the amount of rent collected is a fluctuating figure and that a portion of this money must be applied to operating expenses necessary to keep the project in good running order, they argue that they have the right to collect the rents and to make the decisions as to how the money is best to be applied to expenses and upkeep, and to invest any excess for the benefit of their shareholders.

Plaintiffs point out that they perfected their right to the rents on January 13, 1976, by virtue of the filing of their complaint in this action and, therefore, the only question which arises is to what use should the rents and profits be put during the pendency of these proceedings. They state that the money flowing from the rents cannot be used for the general benefit of the debtor-in-possession because it belongs to these particular secured creditors. Plaintiffs note that the denial

[1]Justice Brandeis in *Wright v. Vinton Branch*, supra, stated: The objection must be tested by "whether as an exercise of the bankruptcy power, for the rehabilitation of the former mortgagor, the Act so far modifies the lienor's right, remedial or substantive . . . to such an extent as to . . . deny the due process of law guaranteed by the Fifth Amendment." Page 442(10) and page 470. The court held that the provisions of the Frazier-Lemke Act to enjoin the foreclosure of farm lands by mortgagees for a period of three years "made no unreasonable modifications of the mortgagee's rights" and the Act was held valid as not arbitrary or unreasonable. He added: "A Court of Bankruptcy may affect the interests of a lien-holder in many ways." *Wright* case, supra, page 470.

of this particular contract right is not necessary to effectuate the purposes of a Chapter XII proceeding. The crux of plaintiffs' argument is that they have a right to the money at this time, that the funds should either be applied to the first mortgage debt or else invested for the benefit of its shareholders, who should be receiving a return on it now, and that the denial of such right to use this property is repugnant to the Fifth Amendment of the Constitution of the United States as a taking of property without due process.

In answer to the complaint for reclamation and termination of the automatic stay filed by the plaintiffs which is to be the subject of a hearing before the Court on March 8, 1976, the debtor contends that the assignment of leases and rents in the security agreement with the plaintiffs is an assignment as "additional security". If, upon a hearing on the merits, the debtor is able to show that the assignment of leases and rents in this case is in fact an assignment as "additional security" as opposed to a present and unconditional assignment, the plaintiffs would not be entitled to any assignment of rents until they are able to show that the primary security, the apartment complex itself, is inadequate to pay the indebtedness. See *Kinnison v. Guaranty Liquidating Corporation, et al.*, 115 P. 2d 450 (1941) and *In Re Cigar Stores Realty Holdings, Inc.*, 69 F. 2d 823 (2d Cir. 1934). Again, there is absolutely no evidence before the Court and the plaintiffs did not undertake at the hearing to produce any evidence that would permit the Court to decide that question. Under these circumstances, there is no basis on which the Court could justify requiring the rentals from the apartment project to be paid over to the plaintiffs.

Also, the Court observes that the present proceeding, which places a fiduciary responsibility upon the debtor-in-possession to pay necessary expenses, has the essential effect of a sequestration if the surplus funds are collected and placed in certificates of deposit for the benefit of the creditors pending ultimate disposition of these proceedings. This Court notes that a debtor-in-possession has a fiduciary duty to apply the funds to the expenses necessary to keep the apartment complex in good running order and it is satisfied at this time that this duty is being carried out by said debtor-in-possession. The appointment of a Chapter XII Trustee has not been requested. If at some time in the future the debtor-in-possession violates his fiduciary responsibility with regard to disbursement and investment of these monies, any creditor can bring that situation to the attention of the Court and request that a trustee be appointed to protect their interest in these monies. This Court is of the opinion that a sequestration right under the contract which would permit secured creditors such as plaintiffs to possess and control all of the funds and to determine how the money should be allocated, either toward expenses and repayment of the secured debt, or toward investments of their own selection, would violate the intent of the rehabilitation intention and objective of Chapter XII of the Bankruptcy Act because such an order would undoubtedly interfere with the right and efforts of the debtor to formulate a plan. However, the Court agrees that any funds that are not absolutely needed for the protection, management and operation of the apartment complex must not be wasted or otherwise expended, but should be protected and held for the benefit of the creditors. Such protection of the creditors and continuation of the business operations of the debtor is the dual objective of the Chapter XII proceeding. The Court notes that while the

plaintiffs may have paramount and superior rights to the funds in question to all other creditors in this proceeding, plaintiffs constitute only one class of secured creditors and this Court will not permit them to exercise sole discretion over the use and disposition of funds collected from rents and profits. Therefore, the debtor-in-possession, defendant Pine Gate, is hereby ordered to invest any surplus funds collected from rents and profits in federally insured savings accounts or certificates of deposit on the best terms reasonably available and hold the income from such investment for the benefit of the creditors and subject to further orders of this Court. Plaintiffs' motion for sequestration of rents and profits is hereby DENIED.

3.

Finally, plaintiffs have moved for an order authorizing them to proceed with publication of notice of sale pursuant to Georgia Code Section 37-607. The essence of their argument in support of this motion is that since plaintiffs have repeatedly stated that they will not approve any plan whatsoever, the only alternative arrangement available under the Bankruptcy Act is to provide full compensation, which will require sale of defendant's sole asset, which is what plaintiffs have been restrained from doing in the first place. It may be true that the plaintiffs will not vote for any Plan of Arrangement in this proceeding. But the announced intention not to do so at the inception of the proceeding and before any Plan has been filed is not sufficient justification for this Court to take any action which might have the effect of depriving the debtor of a fair opportunity to propose a plan for the consideration of its creditors. There is not only the possibility that the plaintiffs may change their minds but there are also other means of dealing equitably with non-assenting creditors.

The petitioner "should be given an opportunity to work out a plan so long as there is any reasonable expectation that such result may be accomplished, even though opposing interest claim in advance that any plan proposed will be futile." 6 Collier on Bankruptcy, Paragraph 6.09, p. 1043 (14th ed. 1972). See *York v. Florida Southern Corp.*, 310 F. 2d 109, 110 (5th Cir. 1962); *In Re Northwest Corp.: Candler v. Higgs & Young, Inc.*, CCH 1975 Bankruptcy Law Reporter, Paragraph 65755, ... F.2d ..... (4th Cir. July 23, 1975). The Court of Appeals for the Fifth Circuit has clearly rejected the contention that the announced opposition of secured creditors to any plan of reorganization which will not provide for complete and immediate payment of the secured creditors may be "a proper basis for defeating Chapter X proceedings at their inception." *Corr v. Flora Sun Corp.*, 317 F. 2d 708, 710 (5th Cir. 1963); cited in *In Re Plaza Towers, Inc.*, 294 F. Supp. 714, 723 (E.D. La. 1967); *but see Janaf Shopping Center, Inc. v. Chase Manhattan Bank*, 282 F. 2d 211, 214 (4th Cir. 1960). Also, an absence of any equity in the value of the property for stockholders in excess of the amount of the secured debt or that the deficiency of value to the debt is increasing continuously is insufficient reason alone to allow foreclosure of the real property of the debtor if the evidence otherwise shows a reasonable expectation of a plan of reorganization being ultimately effected. *Plaza Towers*, p. 719.

In *A-Cos Leasing Corporation v. Wheless*, 422 F. 2d 522 (5th Cir. 1970), the Fifth Circuit, in affirming the district court's dismissal of a Chapter X petition on the grounds that adequate relief could be obtained under Chapter XI, stated:

"The whole scheme of Chapter X indicates that this test should not bar approval of a petition unless it is abundantly clear that there is no possibility that a plan of reorganization can be effected. In other words, *the Court should be 'reorganization minded'* and *not 'liquidation minded.'* Any doubt as to whether a plan can be effected should be resolved in favor of the approval of the petition, as some corporations whose affairs have seemed hopeless at the outset have undergone successful reorganization. In other words, the provisions of Chapter X should be given a sympathetic construction consonant with the relief intended." (Id. at 524). (Emphasis added).

Plaintiffs further note that in the event they prevail at the trial held on March 8, 1976, regarding the stay order, a further delay of sale of four weeks will automatically ensue (due to the fact that they will not be able to begin publication until April 1976) unless advertising is commenced the first week in March. Therefore, plaintiffs contend that the automatic restraining order provided under Rule 12-43 should not be permitted to restrain such publication. Any other result, they argue, constitutes a further taking of a substantive property right from the creditors, which taking is also proscribed by the Fifth Amendment to the United States Constitution.

The Court is of the opinion, however, that in enacting the Chandler Act of 1938, Congress fully understood the impact of the new debtor rehabilitative Chapters X, XI, XII and XIII, and was approving the inherent delays imposed thereby on the normal contractual relationships of the parties. Some delay is inherent in rehabilitative Chapter reorganization and arrangement proceedings and only when these delays run to unwarranted lengths does an abuse develop. The Court finds no such delay in this case up to this point. There is no evidence that the single real estate asset will unreasonably deteriorate in the period projected in this case. The Plan is required to be filed on March 29, 1976, at which time, if filed, a hearing on confirmation of the Plan will be set and notices and ballots sent to creditors. The mere statement by the plaintiffs that they will not accept any plan is not sufficient for this Court to find that any arrangement will be impossible and to torpedo the proceedings at an early stage. And it is this Court's experience that granting permission to advertise before a reasonable period has elapsed after filing to allow the debtor, and *qualified* creditors, to formulate and submit a plan, has the unfortunate effect of limiting debtor's opportunities to revise or reform the enterprise, and chills consideration by the creditors or outsiders of any plans for an arrangement. Therefore, plaintiffs' motion for authorization to begin advertising is hereby denied, orally announced this February 17, 1976, and order entered the date hereinafter stated.

IT IS SO ORDERED, this the ..... day of March, 1976.

WILLIAM L. NORTON, JR.
United States Bankruptcy Judge,
United States Bankruptcy Court,
United States District Court

APPENDIX F

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN THE MATTER OF:

PINE GATE ASSOCIATES, LTD.,
Debtor

GREAT NATIONAL LIFE INSURANCE COMPANY, *et al.*
Appellants

vs.

PINE GATE ASSOCIATES, LTD.,
Appellee

BANKRUPTCY CASE NO. B75-4345A

ORDER

This action is before the court on appeal by secured creditors from the order of March 18, 1976, of the bankruptcy court denying their motions (1) for relief from the effects of an automatic stay pursuant to rule 12-43 of the Bankruptcy Act and for interim orders to compel the debtor to post bond to indemnify the creditors against any diminution of the value of the property subject to their security deed; (2) for the payment of rents and profits; and (3) for an authorization of advertising pursuant to Ga. Code Ann. § 37-607.

Rule 12-43 of the Bankruptcy Act provides that a petition filed under Chapter XII of the Bankruptcy Act shall operate as a stay of any actions by any court for the purpose of enforcing any judgment against the debtor or enforcing any lien against his property. The rule provides that unless terminated, modified, annulled or conditioned by the bankruptcy court, this stay shall remain in force until the termination of the case, conversion to bankruptcy, or abandonment or transfer of the encumbered property. Relief from the stay may be sought by the filing of a complaint, as was done by the secured creditors in this case.

Appellant secured creditors argue that the effect of the stay, which prevents their foreclosing upon the property, is to unconstitutionally deprive them of property without compensation unless the debtor in possession is required to post a bond to protect them against any diminution in value during the pendency of the Chapter XII proceedings. The imposition of the stay under the Bankruptcy Act does not involve the taking of property without compensation in a constitutional sense. *See, e.g., Wright v. Vinton Branch,* 300 U.S. 440 (1937); *John Hancock Mut. Life Ins. Co. v. Casey,* 134 F.2d 162 (1st Cir.) *cert. denied,* 319 U.S. 757 (1943). Appellant secured creditors direct the court's attention to the opinion of Justice Brandeis in *Louisville Joint Stock Land Bank v. Radford,* 295 U.S. 555 (1935). This case involved a provision added to § 75 of the Bankruptcy Act by the Frazier-Lemke Act. The provision found unconstitutional in that case as an unconstitutional taking was amended by Congress and found

constitutional in *Wright v. Vinton Branch,* an opinion also by Justice Brandeis. The provision as amended authorized a stay similar to that involved in a Chapter XII proceeding. Appellants present the novel argument that since they have no intention of approving any plan which the debtor may present, the stay is not justified and under § 461 of the Bankruptcy Act, 11 U.S.C. § 861, the only alternative is complete compensation. At the time this appeal was taken, the debtor had presented no plan. Appellants cite *Kunze v. Prudential Insurance Co. of America,* 106 F.2d 917 (5th Cir. 1939), as authority for their contention that since they will approve no plan, the stay is unjustified. *Kunze* involved a situation in which a plan had been presented and rejected, with no further plan forthcoming. An entirely different situation is presented by the case *sub judice* in which the debtor's plan had not been presented at the time this appeal was taken. Finally, the appellant argues that rule 12-43(d) regarding relief from a stay puts the onus on the party seeking the continuation of the stay to justify it. Appellants contend that the bankruptcy court was mistaken in its determination that in the absence of evidence that the value of the subject property was deteriorating relief from the stay should not be granted. Appellants maintain that the true issue in their motion for relief was whether the property *might* decrease in value during the pendency of the proceedings.

The court finds that the bankruptcy judge was correct in his denial of relief by either lifting the stay or requiring that the debtor post bond for the value of the property. The purpose behind Chapter XII of the Bankruptcy Act is to give the debtor a chance to reorganize and plan for an eventual payment of his debts without the threat of immediate foreclosure or the necessity of going into straight bankruptcy. This policy justifies a temporary denial of access by a secured creditor to his collateral as long as there is no immediately discernible danger of diminution in value of the property. Appellants' concern that fluctuating property values *might* cause such diminution is not sufficient reason to lift the stay. The bankruptcy judge pointed out in his order that appellants have shown no evidence that a bond is necessary to protect them in that they have shown no likelihood that the property will diminish in value. Section 426 of the Bankruptcy Act, 11 U.S.C. 826, provides that the court may require a bond to indemnify the estate against subsequent loss in the event of eventual adjudication of the debtor as a bankrupt. A section 426 bond, even if applicable in this case, is discretionary. Since no evidence was presented that the value of the property is likely to diminish or that a bond could be obtained, the bankruptcy court did not abuse its discretion in refusing to require a bond.

Appellants contend that the bankruptcy court erred in its refusal to sequester or turn over to the appeliants the rents and profits being collected from the apartment complex which represents the debtor's sole asset. Appellants base their argument for sequestration on an agreement between appellants and the debtor entitled Assignment of Leases and Rents which provides that upon default in payment of the debt, appellants have the right to terminate the license granted the debtor to collect the rents. The debtor contends that the assignment was as "additional security" rather than an unconditional security and that appellants would not be entitled to any rents without a showing that the primary security, the apartment complex itself, is inadequate to secure the indebtedness. The

bankruptcy court found that appellants had offered no evidence that the assignment of rents and leases was not "additional security" and found that the court would not be justified in turning these rents over to the appellants. Further, the bankruptcy court found that when no trustee has been requested or appointed, the debtor in possession has a fiduciary responsibility to apply these funds to the maintenance of the primary security, the apartment complex. The debtor is always under the supervision and control of the court, and any abuse of his responsibility can be dealt with by the court. Again, this court cannot find that the bankruptcy court has abused its discretion in refusing to sequester or hand over these rents to appellants.

Finally, appellants contend that the bankruptcy court erred in refusing authorization for immediate advertisement of the property pursuant to Ga. Code Ann. 37-607, again insisting upon their refusal in advance to consent to any plan presented by the debtor. The bankruptcy court correctly concluded that premature advertising would have a chilling effect upon efforts of the debtor to revise and reform the business enterprise, thus thwarting the basic purpose of Chapter XII.

The court finds that the order of March 18, 1976, of the bankruptcy court should be affirmed in all respects.

IT IS SO ORDERED this 19th day of October, 1976.

/s/ WILLIAM C. O'KELLEY
William C. O'Kelley
United States District Judge

APPENDIX G

United States District Court for the NORTHERN District of GEORGIA

FILED IN CLERK'S OFFICE
JAN 22 1976
BEN H. CARTER, Clerk

By: _____
Deputy Clerk

In re

PINE GATE ASSOCIATES, LTD.,

Debtor

Bankrupt (include here all names used by bankrupt within last 6 years)

Bankruptcy No.
B75-4345A

IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII

STATEMENT OF AFFAIRS FOR DEBTOR ENGAGED IN BUSINESS

(Each question should be answered or the failure to answer explained. If the answer is "none," this should be stated. If additional space is needed for the answer to any question, a separate sheet properly identified and made a part hereof, should be used and attached.

If the bankrupt is a partnership or a corporation, the questions shall be deemed to be addressed to, and shall be answered on behalf of, the partnership or corporation; and the statement shall be verified by a member of the partnership or by a duly authorized officer of the corporation.

The term, "original petition," as used in the following questions, shall mean the petition filed under Bankruptcy Rule 103, 104, or 105.)

1. Nature, location, and name of business.

a. Under what name and where do you carry on your business?	(a) Pine Gate Associates, Ltd., % David R. Vaughan, General Partner, 1806 Atlanta Gas Light Tower, 235 Peachtree Street, N.E., Atlanta, Georgia 30303 (This is an address different from the one appearing on the original petition reflecting a relocation proposed prior to the filing of the petition.)
b. In what business are you engaged? (If business operations have been terminated, give the date of such termination.)	(b) Ownership and operation of 118 unit apartment project located at 2454 Beaver Ruin Rd., Norcross, Georgia
c. When did you commence such business?	(c) Fall of 1973

d. Where else, and under what other names, have you carried on business within the 6 years immediately preceding the filing of the original petition herein? (Give street addresses, the names of any partners, joint adventurers, or other associates, the nature of the business, and the periods for which it was carried on.)	(d) None
e. What is your employer identification number? Your social security number?	(e) B158-1158089

2. Books and records.

a. By whom, or under whose supervision, have your books of account and records been kept during the 2 years immediately preceding the filing of the original petition herein? (Give names, addresses, and periods of time.)	(a) Under supervision of David R. Vaughan, General Partner, 1806 Atlanta Gas Light Tower, 235 Peachtree Street, N.E. Atlanta, Georgia 30303
b. By whom have your books of account and records been audited during the 2 years immediately preceding the filing of the original petition herein? (Give names, addresses, and dates of audits.)	(b) Income tax returns prepared by John F. McMullan, CPA Suite 1826, 400 Colony Square, Atlanta, Georgia 30361
c. In whose possession are your books of account and records? (Give names and addresses.)	(c) John F. McMullan, CPA, Suite 1826, 400 Colony Square, Atlanta, Georgia 30361.
d. If any of these books or records are not available, explain.	(d) N/A
e. Have any books of account or records relating to your affairs been destroyed, lost, or otherwise disposed of within the 2 years immediately preceding the filing of the original petition herein? (If so, give particulars, including date of destruction, loss, or disposition, and reason therefor.)	(e) No

3. Financial statements.

Have you issued any written financial statements within the 2 years immediately preceding the filing of the original petition herein? (Give dates, and the names and addresses of the persons to whom issued, including mercantile and trade agencies.)	No

4. Inventories.

a. When was the last inventory of your property taken?	(a) December 27, 1975
b. By whom, or under whose supervision, ... taken?	(b) Ron Allen, Resident Manager
d. When was the next prior inventory of your property taken?	Unknown
e. By whom, or under whose supervision, was this inventory taken?	Unknown
f. What was the amount, in dollars, of the inventory? (State whether the inventory was taken at cost, market or otherwise.)	Unknown
g. In whose possession are the records of the 2 inventories above referred to? (Give names and addresses.)	Unknown

5. Income other than from operation of business.

What amount of income, other than from operation of your business, have you received during each of the 2 years immediately preceding the filing of the original petition herein? (Give particulars, including each source, and the amount received therefrom.)	None

6. Tax returns and refunds.

a. In whose possession are copies of your federal and state income tax returns for the 3 years immediately preceding the filing of the original petition herein?	John F. McMullan CPA, Suite 1806, 400 Colony Square, Atlanta, Georgia 30361
b. What tax refunds (income or other) have you received during the 2 years immediately preceding the filing of the original petition herein?	None
c. To what tax refunds (income or other), if any, are you, or may you be, entitled? (Give particulars, including information as to any refund payable jointly to you and your spouse or any other person.)	None

7. Bank accounts and safe deposit boxes.

a. What bank accounts have you maintained, alone or together with any other person, and in your own or any other name, within the 2 years immediately preceding the filing of the original petition herein? (Give the name and address of each bank, the name in which the deposit was maintained, and the name and address of every person authorized to make withdrawals from such account.)

(a)

(1) National Bank of Georgia, Tucker, Georgia 30081, Pine Gate Apartments Management Account, David R. Vaughan, 1806 Atlanta Gas Light Tower, 235 Peachtree Street, N.E. Atlanta, Georgia 30303, Ruth Goldstein, 1739 Wildwood Road, N.E., Atlanta, Georgia 30306, William L. Kizer, 2455 Beaver Ruin Rd., Apt. 6F, Norcross, Georgia 30071

(2) National Bank of Georgia, Tucker, Georgia 30081, Pine Gate Associates, Ltd. Partnership Account, David R. Vaughan address same as (1) above, Ruth Goldstein, address same as (1) above.

(3) Trust Company of Georgia, Atlanta, Georgia 30303, Pine Gate Associates, Ltd., General Partner Account, David R. Vaughan, address same as (1) above, Ruth Goldstein, address same as (1) above.

b. What safe deposit box or boxes or other depository or depositories have you kept or used for your securities, cash, or other valuables within the 2 years immediately preceding the filing of the original petition herein? (Give the name and address of the bank or other depository, the name in which each box or other depository was kept, the name and address of every person who had the right of access thereto, a description of the contents thereof, and, if the box has been surrendered, state when surrendered or, if transferred, when transferred and the name and address of the transferee.)

(b) None

8. Property held for another person.

What property do you hold for any other person? (Give name and address of each person, and describe the property, the amount or value thereof and all writings relating thereto.)

None

9. Prior bankruptcy proceedings.

What proceedings under the Bankruptcy Act have previously been brought by or against you? (State the location of the bankruptcy court, the nature and number of proceeding, and whether a discharge was granted or refused, the proceeding was dismissed, or a composition, arrangement, or plan was confirmed.)

None

10. Receiverships, general assignments, and other modes of liquidation.

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No

b. Have you made any assignment of your property for the benefit of your creditors, or any general settlement with your creditors, within the 2 years immediately preceding the filing of the original petition herein? (If so, give dates, the name and address of the assignee, and a brief statement of the terms of assignment or settlement.)

No

11. Property in hands of third person.

Is any other person holding, anything of value in which you have an interest? (Give name and address, location and description of the property, and circumstances of the holding.)

Yes — David R. Vaughan — 9/10 acre of real property contiguous to the apartment property — in the name of David R. Vaughan acting as nominee.

12. Suits, executions, and attachments.

a. Were you a party to any suit pending at the time of the filing of the original petition herein? (If so, give the name and location of the court and the title and nature of the proceeding.)

No

b. Were you a party to any suit terminated within the year immediately preceding the filing of the original petiuon herein? (If so, give the name and location of the court, the title and nature of the proceeding, and the result.)

No

c. Has any of your property been attached, garnished, or seized under any legal or equitable process within the 4 months immediately preceding the filing of the original petition herein? (If so, describe the property seized or person garnished, and at whose suit.)

No

13. Payments on loans and installment purchases.

What repayments on loans in whole or in part, and what payments on installment purchases of goods and services, have you made during the year immediately preceding the filing of the original petition herein? (Give the names and addresses of the persons receiving payment, the amounts of the loans and of the purchase price of the goods and services, the dates of the original transactions, the amounts and dates of pay-services, the dates of the original transactions, the amounts and dates of payments, and, if any of the payees are your relatives, the relationship; if the bankrupt is a partnership and any of the payees is or was a partner or a relative of a partner, state the relationship; if the bankrupt is a corporation and any of the payees is or was an officer, director, or stockholder, or a relative of an officer, director or stockholder, state the relationship.)

See Exhibit "B" attached hereto and made a part hereof.

14. Transfers of property.

a. Have you made any gifts, other than ordinary and usual presents to family members and charitable donations, during the year immediately preceding the filing of the original petition herein? (If so, give names and addresses of donees and dates, description, and value of gifts.)

No

b. Have you made any other transfer, absolute or for the purpose of security, or any other disposition which was not in the ordinary course of business during the year immediately preceding the filing of the original petition herein? (Give a description of the property, the date of the transfer or disposition, to whom transferred or how disposed of, and state whether the transferee is a relative, partner, shareholder, officer, or director, the consideration, if any, received for the property, and the disposition of such consideration.)

No

15. Accounts and other receivables.

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No

16. Repossessions and returns.

Has any property been returned to, or repossessed by, the seller or by a secured party during the year immediately preceding the filing of the original petition herein? (If so, give particulars, including the name and address of the party getting the property and its description and value.)

No

17. Business leases.

If you are a tenant of business property, what are the name and address of your landlord, the amount of your rental, the date to which rent had been paid at the time of the filing of the original petition herein, and the amount of security held by the landlord?

Landlord — CRC Joint Venture #4, % David R. Vaughan, Managing Joint Venturer, 1806 Atlanta Gas Light Tower, 235 Peachtree Street, N.E., Atlanta, Georgia 30303. The rental under this lease which related to the real property upon which the partnership's apartment project is located is $1,000 per month. The rental payments were six (6) months in arrears at the time of the filing of the petition. The security held by the Landlord is the secured interest ownership of the real property which is the subject of the lease. The names and addresses of the individual members of CRC Joint Venture #4 are attached hereto and made a part hereof as Exhibit "C".

18. Losses.

a. Have you suffered any losses from fire, theft, or gambling during the year immediately preceding the filing of the original petition herein? (If so, give particulars including dates, names, and places, and the amounts of money or value and general description of property lost.)

(a) Yes, theft of rental office, October 5, 1975, petty cash and several rental payments stolen — $340.00 Washer and dryers — 12/1/75 — $250.00

b. Was the loss covered in whole or part by insurance? (If so, give particulars.)

(b) No — loss was less than deductible.

19. Withdrawals.

a. If you are an individual proprietor of your business, what personal withdrawals of any kind have you made from the business during the year immediately preceding the filing of the original petition herein?

(a) Not applicable

b. If the bankrupt is a partnership or corporation, what withdrawals, in any form (including compensation or loans), have been made by any member of the partnership, or by any officer, director, managing executive, or shareholder of the corporation, during the year immediately preceding the filing of the original petition herein? (Give the name and designation or relationship to the bankrupt of each person, the dates and amounts of withdrawals, and the nature or purpose thereof.)

(b) See Exhibit "D" attached hereto and made a part hereof.

20. Payments or transfers to attorneys.

a. Have you consulted an attorney during the year immediately preceding or since the filing of the original petition herein? (Give date, name, and address.)

(a)(1) Heyman and Sizemore, 3rd Floor, Fulton Federal Bldg., Atlanta, Georgia, 30303, December, 1975

(2) Ms. Charlene Martin, Suite 2004, 400 Colony Square, Atlanta, Georgia, 30361, May 18, 1975

(3) Troutman, Sanders, Lockerman & Ashmore, Candler Bldg., Atlanta, Georgia, 30303, January thru March, 1975

(4) Mr. William E. Bassett, #4 Executive Park Dr., Atlanta, Georgia 30329, December 16, 1975.

b. Have you during the year immediately preceding or since the filing of the original petition herein paid any money or transferred any property to the attorney, or to any other person on his behalf? (If so, give particulars, including amount paid or value of property transferred and date of payment on transfer.)

(b)(1) $3,500.00

(2) $ 317.30

(3) $ 750.00

(4) $1,346.50

c. Have you, either during the year immediately preceding or since the filing of the original petition herein, agreed to pay any money or transfer any property to an attorney at law, or to any other person on his behalf? (If so, give particulars, including amount and terms of obligation.)

(c) None other than the agreement made with Heyman and Sizemore as disclosed in the statement of attorney filed with the Court, said agreement being subject to approval of the Court.

(If the bankrupt is a partnership or corporation, the following additional question should be answered.)

21. Members of partnership; officers, directors, managers, and principal stockholders of corporation.

a. What is the name and address of each member of the partnership, or the name, title and address of each officer, director, and managing executive and of each stockholder holding 25 percent or more of the issued and outstanding stock, of the corporation?

See Exhibit "E" attached hereto and made a part hereof.

b. During the year immediately preceding the filing of the original petition herein, has any member withdrawn from the partnership, or any officer, director, or managing executive of the corporation terminated his relationship, or any stockholder holding 25 per cent or more of the issued stock disposed of more than 50 per cent of his holdings? (If so, give name and address and reason for withdrawal, termination, or disposition, if known.)

No

c. Has any person acquired or disposed of 25 per cent or more of the stock of the corporation during the year immediately preceding the filing of the petition? (If so, give name and address and particulars.)

No

State of GEORGIA
County of FULTON, ss:

I, DAVID R. VAUGHAN, do hereby swear that I have read the answers contained in the foregoing statement of affairs and that they are true and complete to the best of my knowledge, information, and belief.

PINE GATE ASSOCIATES, LTD.

(SEAL)

By: DAVID R. VAUGHAN
General Partner

Debtor

Subscribed and sworn to before me on January 22, 1976

PATSY J. BASWELL
Notary Public
(Official character)

Notary Public, Georgia, State at Large
My Commission Expires Jan. 19, 1980

(Person verifying for partnership or corporation should indicate position or relationship to bankrupt.)

(From the statements of the bankrupt schedules A and B)

SCHEDULE		DEBTS AND PROPERTY	TOTAL
		DEBTS	
Schedule A —	1/a	Wages having priority	$ –0–
Schedule A —	1/b(1)	Taxes owing United States	78.20
Schedule A —	1/b(2)	Taxes owing States	48.74
Schedule A —	1/b(3)	Taxes owing other taxing authorities	21,459.55
Schedule A —	1/c(1)	Debts having priority by laws of the United States	–0–
Schedule A —	1/c(2)	Rent having priority under State law	3,000.00
Schedule A —	2	Secured claims	1,548,838.65
Schedule A —	3	Unsecured claims without priority	28,500.36
		Schedule A total	$1,601,925.50
		PROPERTY	
Schedule B —	1	Real property (total value)	1,981,280.00
Schedule B —	2/a	Cash on hand	36.81
Schedule B —	2/b	Deposits	3,981.73
Schedule B —	2/c	Household goods	–0–
Schedule B —	2/d	Books, pictures, and collections	–0–
Schedule B —	2/e	Wearing apparel and personal possessions	–0–
Schedule B —	2/f	Automobiles and other vehicles	–0–
Schedule B —	2/g	Boats, motors, and accessories	–0–
Schedule B —	2/h	Livestock and other animals	–0–
Schedule B —	2/i	Farming supplies and implements	–0–
Schedule B —	2/j	Office equipment and supplies	1,630.00
Schedule B —	2/k	Machinery, equipment, and supplies used in business	6,649.00
Schedule B —	2/l	Inventory	–0–
Schedule B —	2/m	Other tangible personal property	2,500.00
Schedule B —	2/n	Patents and other general intangibles	–0–
Schedule B —	2/o	Bonds and other instruments	–0–
Schedule B —	2/p	Other liquidated debts	3,300.00
Schedule B —	2/q	Contingent and unliquidated claims	(amt. unknown)
Schedule B —	2/r	Interests in insurance policies	–0–
Schedule B —	2/s	Annuities	–0–
Schedule B —	2/t	Interests in corporations and unincorporated companies	–0–
Schedule B —	2/u	Interests in partnerships	–0–
Schedule B —	2/v	Equitable and future interests, rights, and powers in personality	–0–
Schedule B —	3/a	Property assigned for benefit of creditors	–0–
Schedule B —	3/b	Property not otherwise scheduled	–0–
Schedule B —	4	Property claimed as exempt	–0–
		Schedule B total	$1,999,377.54

United States District Court for the NORTHERN District of GEORGIA

In re

PINE GATE ASSOCIATES, LTD.,

Debtor

Bankrupt (include here all names used by bankrupt within last 6 years)

Bankruptcy No. B75-4345A

IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII

SCHEDULE A. — STATEMENT OF ALL DEBTS OF BANKRUPT

Schedules A-1, A-2, and A-3 must include all the claims against the bankrupt or his property as of the date of the filing of the petition by or against him.

Schedule A-1. — Creditors Having Priority

Nature of claim	Name of creditor and residence of place of business (if known, so state)	Specify when claim was incurred and the consideration therefor; when claim is contingent, unliquidated, disputed, or subject to setoff, evidenced by a judgment, negotiable instrument, or other writing, or incurred as partner or joint contractor, so indicate; specify name of any partner or joint contractor on any debt	Amount of claim $ Cts.
a			
Wages and commissions owing to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt, not exceeding $600 to each, earned within 3 months before filing of petition	NONE		
b			
Taxes owing (itemize by type of tax and taxing authority):	(As of the date of filing of Petition)		
(1) To the United States		For Employee Withholding Taxes	78.20
(2) To any State		Georgia Employee Withholding Taxes	48.74
(3) To any other taxing authority		City of Norcross, Georgia — 1975 taxes	4,234.40
		Gwinnett County, Georgia— 1975 taxes (real)	17,209.44
		(personal)	15.71

		$ Cts.
c		
(1) Debts owing to any person, including United States, entitled to priority by laws of United States (itemize by type)	NONE	
(2) Rent owing to a landlord entitled to priority by laws of any State accrued within 3 months before filing of petition, for actual use and occupancy	Joint Venture #4	3,000.00

Schedule A-2. — Creditors Holding Security

Name of creditor and residence or place of business (if unknown, so state)	Description of security and date when obtained by creditor	Specify when claim was incurred and the consideration therefor; when claim is contingent, unliquidated, disputed, subject to setoff, evidenced by a judgment, negotiable instrument, or other writing, or incurred as partner or joint contractor, so indicate; specify name of any partner or joint contractor on any debt	Market value	Amount of claim without deduction of value of security $ Cts.
1. USLIFE Life Ins. Company of Texas Harry Hines Blvd. at Mockingbird Lane P. O. Box 35844 Dallas, Texas 75235	(Principal Only)	Note dated June 19, 1973 in original principal amount of $828,000 reflecting proceeds of loan for construction of apartment project. Security is a mortgage on the property described on Exhibit "F", said mortgage being dated June 19, 1973.		812,055.70
2. All American Life and Casualty Company 35 East Wacker Drive Chicago, Illinois 60601	(Principal Only)	Note dated June 19, 1973 in original principal amount of $552,000 reflecting proceeds of loan for construction of apartment project. Security is a mortgage on the property described on Exhibit "F", said mortgage being dated June 19, 1973.		541,370.45
3. CRC Joint Venture #4 % David R. Vaughan 1806 Atlanta Gas Light Tower 235 Peachtree Street, N.E. Atlanta, Georgia 30303				138,000.00

		$	Cts.
(The individuals of the joint venture are listed below)			
Mrs. Jody H. Burnett 2354 Havenridge Drive, N.W. Atlanta, Georgia 30305	First National Bank of Atlanta Trustee for Norell Southern Corp. Profit Sharing Plan % Trust Department Real Estate Division P. O. Box 4148 Atlanta, Georgia 30302		
Mrs. Lewis F. Hunter, Jr. P. O. Box 632 Ponte Vedra Beach, Florida 32082	Mr. David D. Machamer, Trustee for Lamont J. Machamer % Mr. Quinn Machamer Dynatron Corp. P. O. Box 20121 Atlanta, Georgia 30325		
Mr. Guy Rutland, III 2317 Sagamore Hills Drive Decatur, Georgia 30033	George W. Statham, M.D. Trustee for Taylor Children 4112 East Ponce de Leon Ave. Clarkston, Georgia 30021		
David R. Vaughan and The First National Bank of Atlanta Co-Trustees U/W of George M. Vaughan First National Bank of Atlanta % Ivan Millender Assistant Trust Officer 2 Peachtree Street, N.E. Atlanta, Georgia 30303			
This claim is based upon the lease agreement described in Item 17 of the Statement of Affairs and consists of $6,000 in rental payments in arrears and $132,000 which is the established purchase price of the fee interest of the real property upon which the apartment project is located as set forth in said lease agreement dated June 1, 1973.			
4. National Bank of Georgia P. O. Box 446 Tucker, Georgia 30084	(Principal Only)	38,412.50	
This is the remaining balance as of January 23, 1975 of a loan made to the partnership. The security for the repayment of this loan is a second mortgage on the real property described in Exhibit "F".			
5. Dan Faulk Faulk Development Co. 4876 Lower Roswell Road Marietta, Georgia 30060		6,333.34	
6. Fidelity Capital Corporation 300 Interstate North, N.W. Atlanta, Georgia		6,333.33	

		$	Cts.
7. First American Invest Corporation 300 Interstate North, N.W. Atlanta, Georgia		6,333.33	
These are notes to individuals or corporations indicated which came into existence on June 19, 1973 as a result of the purchase by the partnership of the property described in Exhibit "G". The security for repayment of said notes is the property described in Exhibit "G".			
	Total	1,548,838.65	

United States District Court for the NORTHERN District of GEORGIA

In re

PINE GATE ASSOCIATES, LTD.,

Debtor

Bankrupt (include here all names used by bankrupt within last 6 years)

Bankruptcy No. B75-4345A

IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII

SCHEDULE B. — STATEMENT OF ALL PROPERTY OF BANKRUPT

Schedules B-1, B-2, B-3, and B-4 must include all property of the bankrupt as of the date of the filing of the petition by or against him.

Schedule B-1. — Real Property

Description and location of all property in which bankrupt has an interest (including equitable and future interests, interests in estates by the entirety, community property, life estates, leaseholds, and rights and powers exercisable for his own benefit)	Nature of interest (specify all deeds and written instruments relating thereto)	Market value of bankrupt's interest without deduction for secured claims listed in schedule A-2 or exemptions claimed in schedule B-4
		$ Cts.
1. 50 year leasehold interest dated June 1, 1973 in the real property described on Exhibit "F" attached hereto and made a part hereof. (Also option to renew lease for an additional 50 years and purchase the fee interest of said property for $132,000.00 until June 1, 1983.) Also, the apartment project improvements located on said property. Said property, in addition to the Lessor's interest, is subject to loans and mortgages in the original principal amounts as follows: (a) $828,000 and $552,000 loans and associated security deeds dated June 19, 1973; (b) assignment of rents dated June 19, 1973; and (c) $38,412.70 loan dated October 6, 1975.		1,956,280.00
2. Fee interest ownership in the real property described on Exhibit "G" attached hereto and made a part hereof. This property is subject to notes and security deeds in the original principal amount of $19,000 dated June 19, 1973. It is also subject to zoning and use restrictions.		25,000.00

Schedule B-2. — Personal Property

Type of property	Description and location	Market value of bankrupt's interest without deduction for secured claims listed on schedule A-2 or exemptions claimed in schedule B-1
		$ Cts.
a. Cash on hand	Petty cash	36.81
b. Deposits of money with banking institutions, savings and loan associations, credit unions, public utility companies, landlords, and others	Balance in bank accounts These are funds held in an escrow account for the payment of taxes by USLIFE Services Co.	2,189.03 1,792.70
c. Household goods, supplies, and furnishings	N/A	
d. Books, pictures, and other art objects; stamp, coin, and other collections	N/A	
e. Wearing apparel, jewelry, firearms, sports equipment, and other personal possessions	N/A	
f. Automobiles, trucks, trailers, and other vehicles	N/A	
g. Boats, motors, and their accessories	N/A	
h. Livestock, poultry, and other animals	N/A	
i. Farming supplies and implements	N/A	
j. Office equipment, furnishings, and supplies	See Exhibit "A" to Statement of Affairs	1,630.00
k. Machinery, fixtures, equipment, and supplies (other than those listed in items j and l) used in business	See Exhibit "A" to Statement of Affairs	6,649.00
l. Inventory	None other than as listed in j., k., and m.	
m. Tangible personal property of any other description	9 washers and dryers subject to terms of leases with tenants	2,500.00
n. Patents, copyrights, franchises, and other general intangibles (specify all documents and writings relating thereto)	None	

Schedule B-2. — Personal Property (Continued)

		$ Cts.
o. Government and corporate bonds and other negotiable and nonnegotiable instruments	None	
p. Other liquidated debts owing bankrupt or debtor	Tenants' rents past due on December 23, 1975	3,300.00
q. Contingent and unliquidated claims of every nature, including counterclaims of the bankrupt or debtor (give estimated value of each)	(1) Centron Corporation — damages for failure to close sale and (2) USLIFE Real Estate Services Corp. as agent for USLIFE Life Ins. Co. of Texas, and All American Life and Casualty Co. — wrongful handling of closing loan	unknown
r. Interests in insurance policies (itemize surrender or refund values of each)	None	
s. Annuities	None	
t. Stocks and interests in incorporated and unincorporated companies (itemize separately)	None	
u. Interests in partnerships	None	
v. Equitable and future interests, life estates, and rights or powers exercisable for the benefit of the bankrupt or debtor (specify all written instruments relating thereto)	None not otherwise diclosed herein	

	ESTIMATED COST
INVENTORY — ADMIN.	
1 Office Desk & Chair	$ 500.00
1 Remington Electric Typewriter	325.00
2 Lamp Tables & 1 Lamp	80.00
1 Bar & 4 Chairs	375.00
2 Card Tables w/4 Chairs each	250.00
3 Wall Pictures	100.00
	$1,630.00
INVENTORY — MAINT.	
Fenced Playground Equipment	$1,000.00
9 sets Kenmore Washer/Dryers @ $310.00	2,790.00
4 Outdoor Picnic Tables	120.00
1 Rug Shampoo Machine	750.00
1 Vacuum Cleaner	350.00
1 Ramrod Street Sweeper	425.00
1 Water Vacuum	350.00
1 Huffy Riding Mower	275.00
2 Push Mowers @ $65.00	130.00
1 Wheelbarrow	35.00
1 16Ft. Ext. Ladder	30.00
1 A-Frame Ladder	30.00
Assortment of Garden Tools	45.00
700lbs. Ice Foe	250.00
100 A/C Filters	58.00
1 Case Lightbulbs	11.00
	$6,649.00
ADMIN.	1,630.00
	$8,279.00

PINE GATE ASSOCIATES, LTD.

Form 8, Page 3, Paragraph 13

CREDITOR NAME & ADDRESS	SECURITY	DATE SECURITY OBTAINED BY CREDITOR	CONSID-ERATION	DATE OF ORIGINAL TRANSACTION
U.S. Life Real Estate Services Corp. Agent For Great National Life Insurance Company All American Life Insurance Company P. O. Box 35266 Dallas, Texas 75235	Mortgage on 118 Unit Apartment bldg. and land 2454 Beaver Ruin Rd. Norcross, Ga.	6/19/73	Cash $828,000	6/19/73 in part
			Cash 552,000	7/ 3/73 in part
National Bank of Ga. (formerly 1st Nat. Bank of Tucker) P. O. 446 Tucker, Ga. 30084	2nd mortgage on 118 unit apartment 2454 Beaver Ruin Rd. Norcross, Ga.	12/14/73	Note	12/14/73
		1/23/75	Note & mortgage	2/28/75
David R. Vaughan 1806 Gas Light Tower 235 Peachtree St., NE Atlanta, Georgia	None	See attached schedule showing advances and repayments of General Partner		
Sears Roebuck & Co. Ponce de Leon Ave. Atlanta, Georgia	Financing Statement	7/14/75	10 washers 10 dryers	

ORIGINAL LOAN	CLAIM AMOUNT	DATE AND AMOUNT OF REPAYMENTS	
$828,000.00	$812,055.70	1/15/75	$11,465.00
		2/ 7/75	11,465.50
		3/ 8/75	11,465.50
552,000.00	541,370.45	4/ 9/75	11,465.50
		5/ 7/75	11,465.50
		6/12/75	13,258.20*
		7/12/75	9,672.80
		8/ 8/75	13,258.20*
30,000.00		1/23/75	1,080.00
		3/ 3/75	1,480.00
43,176.78	38,412.50	3/23/75	1,480.00
		5/30/75	1,450.00
		7/ 1/75	1,450.00
		8/ 2/75	1,450.00
	11,680.00		
		7/ 8/75	625.04
		7/23/75	18.27
		9/ 9/75	651.04
		10/ 7/75	1,932.32

* Of these payments, $1,792.70 is held in escrow by U.S. Life Real Estate Services Corp. for payment of taxes.

EXHIBIT "B"

DRV — ADVANCES TO
(Pine Gate)

DATE	CHECK #	PAYMENT	RUNNING TOTAL	REIM.	RUNNING TOTAL	BALANCE DUE DRV
4-12	2,486	50.00	50.00			50.00
5-24	2,593	1,107.16	1,157.16			1,157.16
6-17	2,650	1,570.00	2,727.16			2,727.16
7- 2	2,653	9,200.00	11,927.16			11,927.16
7- 2				2,500.00	2,500.00	9,427.16
7-11	2,685/86	4,000.00	13,427.16			13,427.16
7-17	2,688	1,370.00	14,797.16			14,797.16
8- 1	2,756	1,370.00	16,167.16			16,167.16
8-22	2,790	875.00	17,042.16			17,042.16
9-18	223			15,000.00		2,042.16
9-18	2,854	3,250.00				5,292.16
10-31	2,950	1,335.00				6,627.16
11-11	2,963	875.00				7,503.16
11-19		1,330.00				8,832.16
11-17		1,330.00				10,162.16
12-31	3,095	3,000.00				13,162.16
12-30	3,084	11,000.00				24,162.16
1975						
1-15				5,000.00		19,162.16
1-24				6,000.00		13,162.16
2-20		1,705.00				14,867.16
3-10	226	750.00				15,617.16
3-19		1,455.00				17,072.16
3-21		100.00				17,172.16
4-17		1,500.00				18,672.16
5-16	365	2,500.00				21,172.16
5-21		275.00				21,447.16
6-16	428	4,400.00				25,847.16
7- 2	from Apt. Acct.			1,200.00		24,647.16
7-24		3,000.00				27,647.16
8-19		2,500.00				30,147.16
8-22		257.00				30,005.34
8-24		500.00				31,305.34
8-26		650.00				31,955.34
8-27	pd. in daily Comm.	100.00				32,080.34
9- 4		25.00				32,090.34
9- 9				5,000.00		27,080.34
10- 6				2,500.00		24,580.34
10- 1		300.00				24,880.34

DRV — ADVANCES TO
(Pine Gate)

DATE	CHECK #	PAYMENT	RUNNING TOTAL	REIM.	RUNNING TOTAL	BALANCE DUE DRV
4-12	2,486	50.00	50.00			50.00
5-24	2,593	1,107.16	1,157.16			1,157.16
6-17	2,650	1,570.00	2,727.16			2,727.16
7- 2	2,653	9,200.00	11,927.16			11,927.16
7- 2				2,500.00	2,500.00	9,427.16
7-11	2,685/86	4,000.00	13,427.16			13,427.16
7-17	2,688	1,370.00	14,797.16			14,797.16
8- 1	2,756	1,370.00	16,167.16			16,167.16
8-22	2,790	875.00	17,042.16			17,042.16
9-18	223			15,000.00		2,042.16
9-18	2,854	3,250.00				5,292.16
10-31	2,950	1,335.00				6,627.16
11-11	2,963	875.00				7,503.16
11-19		1,330.00				8,832.16
11-17		1,330.00				10,162.16
12-31	3,095	3,000.00				13,162.16
12-30	3,084	11,000.00				24,162.16
1975						
1-15				5,000.00		19,162.16
1-24				6,000.00		13,162.16
2-20		1,705.00				14,867.16
3-10	226	750.00				15,617.16
3-19		1,455.00				17,072.16
3-21		100.00				17,172.16
4-17		1,500.00				18,672.16
5-16	365	2,500.00				21,172.16
5-21		275.00				21,447.16
6-16	428	4,400.00				25,847.16
7- 2	from Apt. Acct.			1,200.00		24,647.16
7-24		3,000.00				27,647.16
8-19		2,500.00				30,147.16
8-22		257.00				30,005.34
8-24		500.00				31,305.34
8-26		650.00				31,955.34
8-27	pd. in daily Comm.	100.00				32,080.34
9- 4		25.00				32,090.34
9- 9				5,000.00		27,080.34
10- 6				2,500.00		24,580.34
10- 1		300.00				24,880.34

DRV — ADVANCES TO
(Pine Gate)

DATE	CHECK #	PAYMENT	REIM.	BALANCE DUE DRV
				24,880.34
8- 5			1,200.00	23,680.34
11-17			4,000.00	19,680.34
12- 4			4,000.00	15,680.34
12-18			4,000.00	11,680.34

CRC JOINT VENTURE #4

INVESTOR

Mrs. Jody H. Burnett
2354 Havenridge Drive, N. W.
Atlanta, Georgia 30305

First National Bank of Atlanta
Trustee for Norrell Southern Corp.
Profit Sharing Plan
% Trust Department
Real Estate Division
P. O. Box 4148
Atlanta, Georgia 30302

Mr. Lewis F. Hunter, Jr.
P. O. Box 632
Ponte Vedra Beach, Florida 32082

Mr. David D. Machamer, Trustee
for Lamont J. Machamer
% Mr. Quinn Machamer
Dynatron Corp.
P. O. Box 20121
Atlanta, Georgia 30325

Mr. David D. Machamer, Trustee
for Lisa S. Machamer
% Mr. Quinn Machamer
Dynatron Corp.
P. O. Box 20121
Atlanta, Georgia 30325

Mr. Guy Rutland, III
2317 Sagamore Hills Drive
Decatur, Georgia 30033

George W. Statham, M. D.
Trustee for Taylor Children
4112 East Ponce de Leon Ave.
Clarkston, Georgia 30021

David R. Vaughan and
The First National Bank of Atlanta
Co-Trustees U/W of George M. Vaughan
First National Bank of Atlanta
% Ivan Millender
Assistant Trust Officer
2 Peachtree Street, N. E.
Atlanta, Georgia 30303

EXHIBIT "C"

PINEGATE ASSOCIATES, LTD.

LIMITED PARTNERS

Mr. Raymond E. Alden
Alexander-Seewald Co.
P. O. Box 93626
Atlanta, Georgia 30318

Donald Boersma, M. D.
7029 Oakbrook, S. E.
Grand Rapids, Michigan 49506

Mr. Harold L. Brander, Jr.
230 Union Bank Plaza
Grand Rapids, Michigan 49502

Mr. and Mrs. Robert J. Brown
1831 Torquay
Royal Oak, Michigan 48073

Mrs. Jody H. Burnett
2354 Havenridge Drive, N. W.
Atlanta, Georgia 30305

Mr. S. Donald English
Route #2, Azalea Circle
Swainsboro, Georgia

Mr. William F. English
Golf Drive
Swainsboro, Georgia

Mr. Gerald S. Eplee
2926 Portage Street
Kalamazoo, Michigan 49001

Mr. and Mrs. D. Richard Grosser
Route #3, Box 182
Vicksburg, Michigan 49097

Mr. Charles D. Lewis, Jr.
Lewis Sales Company
2520 Leslie Drive, N. E.
Atlanta, Georgia 30345

LIMITED PARTNERS

Mr. Alfred Moses
P. O. Box 749
Washington, Georgia 30673

Mr. C. W. Patterson
President
Southern Gunite Flooring
Company, Inc.
1411 Dalon Drive, N. E.
Atlanta, Georgia 30306

Mr. James D. Moye
1800 Peachtree Street, Suite 200
Atlanta, Georgia 30309

Mr. Leonard M. Newman
89 Monroe Avenue
Grand Rapids, Michigan 49502

Mr. Henry J. Roehrich
1206 E. High Street
Mt. Pleasant, Michigan 48858

Mr. Vincent E. Rohrs
755 Old Kent Building
Grand Rapids, Michigan 49502

Mr. Richard L. Scholl
2923 Maple Street
Michigan City, Indiana 46360

GENERAL PARTNER

Mr. David R. Vaughan
1806 Atlanta Gas Light Tower
235 Peachtree Street
Atlanta, Georgia

EXHIBIT "E"

PINE GATE ASSOCIATES, LTD.

Form 8, Page 4, Paragraph 19b

Name of Recipient	Purpose of Distribution	Relation of Recipient to Debtor	Date	Amount
David R. Vaughan	Guaranteed General Partners fee — proceeds of capital contribution from limited partners	General Partner	2/19/75	$17,696.70
David R. Vaughan	Repayment of loans (advances) to Debtor by General Partner	General Partner	See schedule attached to Exhibit "B" in answer to question No. 13	
David R. Vaughan	Administrative fee for 1974 and 1975	General Partner	12/18/75	2,000.00
David R. Vaughan (Payment was actually made to W. E. Carroll Co. as a management fee for the apartment project)	Management fee	General Partner David R. Vaughan as agent for management company received one-half of fee for services rendered to the management company	9/15/75 10/ 4/75 11/ 3/75 11/ 7/75 12/18/75	500.00 500.00 500.00 500.00 500.00

EXHIBIT "D"

ALL that certain real estate situated and being in Land Lots 225, 241 and 242 of the 6th District, County of Gwinnett, State of Georgia, to-wit:

BEGINNING at an iron pin located on the southwesterly right of way line of Beaver Ruin Road (130 foot right-of-way), said iron pin also marking the northeasterly property corner of land now or formerly owned by Beard, et al, and running thence south 10 degrees 53 minutes 00 seconds west 260.2 feet to an iron pin; running thence south 31 degrees 55 minutes west, 834.40 feet to an iron pin; running thence south 58 degrees 48 minutes west, 159.7 feet to an iron pin; running thence south 10 degrees 26 minutes east 552.30 feet to an iron pin; running thence north 73 degrees 48 minutes east, 152.50 feet to an iron pin; running thence north 24 degrees 48 minutes east 967.80 feet to an iron pin; running thence north 10 degrees 53 minutes 00 seconds east, 296.86 feet to a point; running thence north 79 degrees 07 minutes 00 seconds west, 121.33 feet to a point; running thence north 10 degrees 53 minutes 00 seconds east, 344.06 feet to a point on the southwesterly right-of-way line of Beaver Ruin Road (130 foot right-of-way); running thence along the said right-of-way line of Beaver Ruin Road north 59 degrees 00 minutes 00 seconds west, 31.96 feet to an iron pin and the Point of Beginning, as shown on surveys for Beaver Ruin Associates, Inc. dated May 8, 1973, and May 22, 1973, respectively and prepared by Milton R. Lemon, Georgia Registered Land Surveyor.

EXHIBIT "F"

All that tract or parcel of land lying and being in Land Lots 241 and 242 of the 6th District of Gwinnett County, Georgia, and being more particularly described as follows:

TO FIND THE POINT OF BEGINNING, BEGIN at an iron pin located on the southwesterly right-of-way line of Beaver Ruin Road (130 foot right-of-way), said iron pin also marking the northeasterly property corner of land now or formerly owned by Beard, et al; run thence along the said right-of-way line of Beaver Ruin Road south 59 degrees 00 minutes 00 seconds east, 31.96 feet to a point on said right-of-way line of Beaver Ruin Road, which is the POINT OF BEGINNING; run thence south 10 degrees 53 minutes 00 seconds west, 344.06 feet to a point; run thence south 79 degrees 07 minutes 00 seconds east, 121.33 feet to a point; run thence north 10 degrees 53 minutes 00 seconds east, 303.14 feet to an iron pin on the southwesterly right-of-way line of Beaver Ruin Road (130 foot right-of-way); run thence along said right-of-way line of Beaver Ruin Road north 60 degrees 28 minutes 45 seconds west, 128.05 feet to a point which is the Point of Beginning.

EXHIBIT "G"

NAME	AMOUNT DEPOSIT RCVD.	NAME	AMOUNT DEPOSIT RCVD.
Partain	$ 100.00	Painter	$ 100.00
Mitchell	100.00	Mason	100.00
Baldwin	100.00	Allen	100.00
Ray	100.00	Steward	100.00
Steedley	100.00	Wetzel	100.00
Barnett	100.00	Hollis	100.00
Katzen	100.00	Kaiser	100.00
Searcy	100.00	Wehunt	100.00
Frather.	100.00	Ross	100.00
Smith	100.00	Black	100.00
Rabren	100.00	Davis	100.00
Ivey	100.00	Creswell	100.00
Cannon	100.00	Norris	100.00
Fricks	100.00	McWaters	100.00
Coker	100.00	Reese	100.00
Downs	100.00	Antico	100.00
Hill	100.00	Sammons	100.00
Guess	100.00	DiGiovanni	100.00
London	100.00	Surman	100.00
Drake	100.00	Griffin	100.00
Porter	100.00	Lindsay	100.00
Smith	100.00	Raisinghani	100.00
Phillips	100.00	Williams	100.00
Johnson	100.00	Towry	100.00
Ethridge	100.00	Hudson	100.00
Jaecksch	100.00	Myford	100.00
Hathaway	100.00	Shimp	100.00
Christensen	100.00	Hardin	100.00
White	100.00	Sorrells	100.00
Henry	100.00	Jackson	100.00
Smith	100.00	Smalley	100.00
Morris	100.00	Goodwin	100.00
Hamby	100.00	Branua	100.00
Kelsey	100.00	Smith	100.00
Sosebee	100.00	Sellers	100.00
Sullivan	100.00	Adams	100.00
Carter	100.00	Johnson	100.00
Adkins	100.00	Hensley	100.00
Power	100.00	Peterson	100.00
Scott	100.00	Stewart	100.00
Ford	100.00	Schroder	100.00
Caugh	100.00	Irmscher	100.00
Radaway	100.00	Mack	100.00
Newport	100.00	Roman	100.00
Creason	100.00	Burke	100.00
Runke	100.00	Hamilton	100.00
			$9,200.00

EXHIBIT "H"

Schedule A-3. — Creditors Having Unsecured Claims Without Priority

	Name of creditor (including last known holder of any negotiable instrument) and residence or place of business (if unknown, so state)	Specify when claim was incurred and and the consideration therefor; when claim is contingent, unliquidated, disputed, subject to setoff, evidenced by a judgment, negotiable instrument, or other writing, or incurred as partner or joint contractor, so indicate; specify name of any partner or joint contractor on any debt	Amount of claim
			$ Cts.
1.	Atlanta Gas Light Tower Co. 89 Annex Atlanta, Georgia 30389	Utility service — open account	2,639.18
2.	Atlanta Rotary DeRooting P. O. Box 36119 Decatur, Georgia 30032	11/27/75 — sewer services	53.00
3.	Axtell-Williams & Assoc. Suite 117 1699 Tullie Circle, N.E. Freeway Office Park Atlanta, Georgia 30329	Collection agency — 12/1/75	92.96
4.	William L. Kizer Apt. 6F 2455 Beaver Ruin Road Norcross, Ga. 30071	Painting services — Nov./Dec., 1975	100.00
5.	Marvin F. Poer & Co. Suite 588 Century Center 2200 Century Parkway, NE Atlanta, Ga. 30345	Consultant Services — Open Account	208.34
6.	John F. McMullan, CPA Suite 1826 400 Colony Square Atlanta, Georgia 30361	12/16/75 — Accounting Services	180.10
7.	Oxford Chemicals P. O. Box 100710 Atlanta, Ga. 30384	Supplies — Open Account	365.60
8.	Patterson Waste & Equipment 3905 White Oak Lane Lilburn, Ga. 30247	Monthly trash disposal — open acct.	250.00
9.	Poolside, Inc. 6518 Interstate 85 Norcross, Ga. 30071	Servicing pool — 1974	437.32
10.	Print Shop Colony Square 1175 Peachtree St., NE Atlanta, Ga. 30361	Printing Supplies — open acct.	7.70
11.	Southern Bell P. O. Box 100051 Atlanta, Georgia 30348	Telephone Services — open acct.	65.27

Schedule A-3. — Creditors Having Unsecured Claims Without Priority (Continued)

			$ Cts.
12.	Telechem Corp. P.O. Box 28818 Atlanta, Ga. 30328	Supplies — open acct.	366.38
13.	Trimble House Corp. P. O. Box 726 Norcross, Ga. 30071	Tubing — Dec. 4, 1975	82.40
14.	David R. Vaughan General Partner 1806 Gas Light Tower 235 Peachtree St., NE Atlanta, Georgia	Advances in 1975	11,630.84
15.	Troutman, Sanders, Lockerman & Ashmore Candler Building Atlanta, Ga. 30301	Legal Services — 1973 and 1974	2,500.00
16.	Security Deposits from residents	See attached list, Exhibit "H"	9,200.00
17.	Diahn's Executive Telephone Answering Service 1312 Spring Street Smyrna, Ga. 30080	Open account	33.00
18.	First Quality Exterminating Service 5269 Buford Highway Atlanta, Ga. 30340	Termite inspection — 11/19/75	188.00
19.	Kem Manufacturing Corp. 2075 Tucker Industrial Rd. Tucker, Ga. 30084	Cleaning chemicals — open acct.	100.27
		TOTAL	$28,500.36

APPENDIX H

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN THE MATTER OF PINE GATE ASSOCIATES, LTD., Debtor	IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII
GREAT NATIONAL LIFE INSURANCE COMPANY, formerly U.S. Life, LIFE INSURANCE COMPANY OF TEXAS, and ALL AMERICAN LIFE AND CASUALTY COMPANY, Plaintiffs v. PINE GATE ASSOCIATES, LTD., Defendant	CASE NO. B-75-4345A FILED IN CLERK'S OFFICE JUL 1 1976 Ben H. Carter, Clerk By FLP Deputy Clerk

ORDER

This matter is presently before the Court on a complaint of Great National Life Insurance Company, formerly U.S. Life, Life Insurance Company of Texas, and All American Life and Casualty Company (hereinafter referred to collectively as "U.S. Life") for an Order relieving injunction, authorizing foreclosure of deeds to secure mortgage, for an order sequestering rents, issues and profits, and for relief from effects of automatic stay, to which the defendant, Pine Gate Associates, Ltd. filed a timely answer and counterclaim for damages suffered by it as a result of the alleged wrongful conduct of U.S. Life. This matter was heard initially on April 1, 1976, and said hearing was continued thereafter at two subsequent sessions on April 5, 1976 and April 20, 1976.

The Court previously took this matter under advisement, and having considered the evidence presented by the parties during the course of said hearing, and those pleadings which are a part of the record in this matter, the Court makes the following findings of fact and conclusions of law based thereon.

FINDINGS OF FACT

Pine Gate Associates, Ltd. (hereinafter called "Pine Gate") is a limited partnership organized and existing under the laws of the State of Georgia, and Mr. David R. Vaughan is the general partner thereof. Pine Gate is engaged in the business of owning and operating apartments known as Pine Gate Apartments and located in Gwinnett County, Georgia.

On December 23, 1975, Pine Gate filed a petition for an arrangement under the provisions of Chapter XII of the Bankruptcy Act in this Court, and was and is at all times material to this matter a Debtor in Possession under the provisions of the Bankruptcy Act and Bankruptcy Rules of Procedure.

The apartment project known as Pine Gate Apartments, and described with particularity in Plaintiffs' Complaint and the deed to secure debt attached thereto as Exhibit "C" is an asset of Pine Gate over which this Court exercises jurisdiction as a result of the pendency of the aforementioned Chapter XII petition.

Plaintiffs are the holders of two promissory notes executed by Pine Gate by Mr. David R. Vaughan, General Partner, and dated June 19, 1973, which notes are secured by a deed to secure debt held by U.S. Life, which is recorded at Book 683, page 225, records of the Clerk of Superior Court of Gwinnett County, Georgia.

Plaintiffs are also the holders of an assignment of leases and rents from the Pine Gate Apartment Project, which is designed to provide additional security to Plaintiffs to further secure the repayment of the promissory notes hereinabove stated which are primarily secured by the deed to secure debt.

Both promissory notes and the deed to secure debt contain a so-called 'exculpatory clause" whereby Pine Gate, Mr. Vaughan, as its general partner, and all persons associated with Pine Gate are absolved from any personal liability on said notes, it being the intention of the parties to the notes and security deed (Pine Gate and U. S. Life) that the debt evidenced by said promissory note be secured solely by the value of the Pine Gate Apartment project rather than the personal financial wherewithall of Mr. Vaughan or any other assets of Pine Gate or any parties interested therein.

The Pine Gate Apartment Project began operation in mid-1973, at a point in time at which the now well documented recession in the real estate market was just beginning. Moreover, Pine Gate Apartments entered a market area which contained a number of other apartment complexes, several of which unfortunately also commenced operations concurrently with the time at which Pine Gate began operating.

Due to the economic recession in the greater Atlanta area during the months immediately following the commencement of its operations (including unemployment, the oil embargo, increased automobile fuel costs and threats of rationing) Pine Gate, located in the Norcross area some 3 miles north of the perimeter highway around Atlanta, suffered a lower occupancy rate than had been expected or anticipated by either Pine Gate or U. S. Life. Additionally, due to the fact that Pine Gate was designed to operate as a "utilities paid" apartment complex, the revenue produced from its leases was considerably lower than that which had been anticipated by either Pine Gate or U.S. Life due to the extraordinary escalation of costs of utility services.

The net result of this phenomenon was that the Pine Gate Apartment complex was unable to make the payments required under the terms of its promissory notes with the Plaintiffs and pay its other operating expenses, and, therefore, it filed the present Chapter XII proceeding.

During the course of this Chapter XII proceeding, and up to the date of the final hearing on Plaintiffs' Complaint, Pine Gate had begun to cure its economic and perhaps managerial, problems. The occupancy rate of its apartments had begun to increase slightly; it had employed a management company, Southern Heritage Management, Inc., whose chief executive officer has had significant experience in working with financially troubled or distressed properties, and

it had begun to take action to complete those items of deferred maintenance which it was unable to do prior to filing the Chapter XII petition. It was agreed by all parties to this matter that the performance of these deferred maintenance items was something which was needed and which would have to be done regardless of who owned or was responsible for the operation of the apartment complex.

In addition to the improvement in Pine Gate's own operations, the apartment market in the area of Pine Gate is also improving at a steadily discernable rate. The level of occupancy in the entire greater Atlanta area is increasing by one-half to one percent per month, and the occupancy level in the Norcross area (of which Pine Gate is a part) is increasing at a somewhat higher rate. Family increases in Gwinnett County and more particularly in the two mile radius of Norcross, and between Peachtree Corners and Interstate Highway 85 which surrounds this centrally located property, near schools and shopping areas, exceed family increases in other greater Atlanta areas. No new apartment or condominium construction is known to be scheduled within 1976. The surplus of available apartments in the Norcross-Pine Gate area is steadily decreasing, and within a relatively short period of time during 1976 the market should be "saturated" to the point that people seeking apartments in that area will be required to fill or substantially fill the existing apartment units, including those at Pine Gate.

In addition to these market factors, which point to the conclusion that there will in all probability be an increase in both revenues and occupancies for the Pine Gate project, the Court also finds that this Pine Gate project is essential to the continued operation of the business of the Debtor, which consists exclusively of owning and operating this apartment project.

With regard to the revenues generated and to be generated by the Pine Gate Apartment complex since the filing of the Chapter XII petition, these monies are being placed in a fund over which this Court exercises direct supervision and control, and to the best of this Court's knowledge, said funds have been used exclusively in the operation and maintenance of the Pine Gate Apartment project. There is no evidence before the Court to suggest that any monies so generated have been used for any purposes other than the maintenance or enhancement of this project, and any such expenditures which have been made have been necessary for the continued operation of this project.

If Plaintiffs were allowed to foreclose on the Pine Gate property today, they would, according to their own witnesses, realize an amount substantially less than the face amount of their promissory notes, and would not, in all likelihood, ever be able to realize the face amount of these notes. Furthermore, since Plaintiffs are insurance companies, Plaintiffs would undoubtedly incur the same type expenses as those which are being incurred in the operation of the apartment project under the supervision of this Court. The testimony was that Plaintiffs would probably operate the facility through an apartment management company similar to Southern Heritage Management, Inc. recently engaged by the Debtor.

With regard to the counterclaim filed by the Defendant Pine Gate in this matter, the Court makes the following additional findings of fact.

The letter of commitment issued to the predecessor in interest to Pine Gate from the Plaintiffs contained no requirement that the .9 acres fronting the Pine Gate

Apartment project be included in the security or contained any restrictions as to use; nevertheless, the ultimate provision in the deed to secure debt securing the promissory notes hereinabove described requires a restrictive covenant to be placed upon such usage by Mr. Vaughan, the General Partner of Pine Gate. In order to obtain this restrictive covenant the Plaintiffs wrongfully refused to fund the so-called "floor loan", which was the initial funding of the permanent financing required by the terms of the commitment letter which inured to the benefit of Pine Gate.

Moreover, there is no restriction in said commitment letter which would preclude Pine Gate from entering into leases for a period longer than 12 months which contained rent concessions, but which nevertheless required the payment of full rent for a one year period. In fact, it appeared from the testimony of several of the witnesses presented by both Plaintiffs and Defendant that the giving of rent concessions is a valid and acceptable means of securing occupancy in either new apartment projects or those which might be having an occupancy problem.

Although such leases were not prohibited by the commitment, Plaintiffs nevertheless wrongfully delayed the closing of the "ceiling" portion of the permanent financing. After the delay, they eventually did accept the leases in question.

As a direct and proximate result of these wrongful acts by Plaintiffs, Defendant, Pine Gate, suffered damages in the total amount of $22,477.82, made up of the following increments: $13,800.00 — forefeiture of good faith deposit to lender; $4,214.00 — extra interest on construction loan with the Barnett Bank; $125.00 — cost of airplane ticket for attorney to travel to New York; $1,015.36 — differential in interest rate between interest on "gap loan" and permanent loan interest; $2,400.00 — additional work required by staff of general partner and general partner to cure difficulties caused by Plaintiffs' actions; $160.00 — additional long distance telephone calls caused by Plaintiffs' actions; and $688.26 — additional interest on "gap loan".

CONCLUSIONS OF LAW

In determining whether or not to grant the relief requested by a secured creditor, such as the Plaintiffs in this case, a Court, in a rehabilitation proceeding under the Bankruptcy Act, must be guided by its equitable discretion. *Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific Railway Co.*, 294 U.S. 648 (1935).

In exercising this discretion, this Court believes that it is significant to consider that the purposes of a rehabilitative proceeding under the Bankruptcy Act differs substantially from that of a straignt bankruptcy in that the purpose of a rehabilitative proceeding is not to liquidate the assets of a bankrupt in order to pay his creditors and free him of accumulated debts; rather, the purpose of a reorganization is to save a sick business, not to bury it and divide up its belongings. *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783.

Moreover, to accomplish the rehabilitative purposes of Chapters X, XI or XII of the Bankruptcy Act, a Debtor must be given the opportunity to operate its business during the course of the proceeding in such a manner as to be able to propose to its creditors a Plan of Arrangement which, by law, would include

the alteration or modification of the rights of creditors holding debts secured by liens on real estate or chattels real of which the Debtor is the legal or equitable owner. *In Re: Potts*, 47 F. Supp. 990, 142 F.2d 883, cert. denied 324 U.S. 868. The purpose of a Chapter XII proceeding, in particular, is to provide relief for a Debtor in order that it may be permitted to pay creditors over a period of time while continuing to operate the estate as a going business. *In Re: Pittsburgh Duquesne Development Co.*, 327 F.Supp. 1194, *In Re: Dick*, 296 F.2d 912.

To state the matter succinctly, the whole point of a Chapter XII Proceeding is to allow the Debtor to continue to operate its business and remain in possession of its property, and in determining whether a secured creditor is entitled to the relief such as that sought by Plaintiffs, this Court must weigh heavily the purposes of this proceeding. In consideration of these rehabilitative concepts, the Court concludes, in its equitable discretion, that Plaintiffs are not, at this time, entitled to any of the relief sought.

A. COMPLAINT TO FORECLOSE

As to that relief requested by Plaintiffs which would allow them to exercise whatever power they might have to sell the Pine Gate Apartment project under the deed to secure debt held by them, this Court concludes that such an action would have an irreparably harmful effect upon the prospects of rehabilitation of this Debtor. Obviously, from the facts found above, the apartment project is absolutely essential to the continued operation of the business of Pine Gate and to permit foreclosure absolutely prevents any possibility of rehabilitation. This factor, in and of itself, is a critical factor in determining whether to grant Plaintiffs the relief requested. See *In Re: Commonwealth Bond Corporation*, 77 F.2d 308.

The evidence shows that since completion of the project and closing of the loan, the value of the property has decreased partly by depreciation, the apartments are, of course, older than when completed several months ago, maintenance has not been adequate and the project is in need of some superficial face-lifting and repair; but mostly the decrease in value has been in terms of the experience of general depressed economic conditions, insufficient gross receipts brought on by insufficient numbers of tenants, and the unanticipated gross increases in utility costs amid the fuel crisis. The adverse effects, resulting from the delay incident to the Chapter XII action and the inability of the creditor to reclaim the property under the terms of the loan agreement is a concern of the court in making its determination whether the rights of the creditor to due process are being offended by the injunction and continuation of the Chapter XII proceeding. If such constitutional rights of the creditor beyond its rights under the loan agreement are being offended by the Chapter XII proceeding, that is, the creditor is being irreparably harmed, even though the property is necessary to debtor to formulate a plan to continue its business, and there is no reasonable likelihood of a reorganization, the prayers of plaintiff to lift the restraint upon foreclosure should be granted to permit recovery of the real property pursuant to the terms of the loan agreement. This Chapter XII proceeding was conceived by Congress to achieve rehabilitation of a financially harrassed unincorporated debtor so that the debtor may, within a reasonable period, come to an accord with the classes of creditors

contemplated in Chapter XII, propose an arrangement, comply with the promises made in the arrangement, and thereby emerge as a viable business enterprise. It is the duty of the court to consider the balance of the hurts among the parties in this proceeding to determine whether the actual harm of the stay against the secured creditor exceed the statutory purpose of Chapter XII and the rights of the debtor granted by Congress for rehabilitative relief. Whatever criteria are applied by the court to determine whether the stay should be modified and the secured creditor permitted to foreclose, should bear a rational basis to the objective of the proceedings, the balance of the hurt between the parties, the nature of the interests to be protected and the overall congenial statutory purpose of Chapter XII. *In re Groundhog Mountain Corporation,* S.D.N.Y., May 6, 1975, Bankruptcy Judge Babitt.

The evidence reasonably suggests that a possible reorganization would achieve a greater return to the creditor on its debt than would a forced sale.

The court concludes that the creditor has not shown that the value of the property has decreased since the filing of the petition and that the creditor is being further harmed by this proceeding.

There is evidence that the depressed economic conditions and the occupancy rate are improving since the filing of the petition. The court concludes from all the evidence that whatever hurts have occurred to the creditor in the decrease of the value of its security prior to the filing of this petition have not increased since the filing.

Moreover, since this Court believes that the Debtor is entitled, at this stage of the proceedings,[1] to every reasonable opportunity to seek to rehabilitate its

[1]The Plaintiffs have in no sense been deprived of procedural due process in this case. They have participated extensively and have had full opportunity to be heard. The Chapter XII petition was only filed on December 23, 1975. Less than one month later, on January 14, 1976, the Plaintiffs filed their complaint for an order lifting the stay, permitting foreclosure and sequestering rents. Prior to a hearing on that complaint, Plaintiffs filed motions to compel sequestration of rents, a bond to indemnify against diminution in value of their security, an order authorizing advertising pending a ruling by the Court on the complaint to foreclose. On February 10, 1976, the First Meeting of Creditors was held at which Plaintiffs examined the Debtor. On February 17, 1976, the Bankruptcy Court held a hearing on Plaintiffs motions. The decision of said Court was orally announced on said date not to grant the motions and a formal Order was entered on March 19, 1976. Plaintiffs appealed that Order to the District Court where it is now pending. On April 1, 5, and 20, the Bankruptcy Court conducted a total of approximately 12 hours of hearings on Plaintiffs complaint. The Debtor filed its proposed Plan of Arrangement with the Court on May 14, 1976 and the hearing on confirmation was held on May 27, 1976. Five classes of creditors voted in favor of the Plan of Arrangement and only the class of secured creditors consisting solely of Plaintiffs voted against the Plan of Arrangement. Substantial legal issues were presented by the contentions of Plaintiffs and the Debtor relating to the confirmation of said Plan of Arrangement and application of Section 461 (11)(c) of the Bankruptcy Act. 11 U.S.C. § 861 (11)(c). Briefs were filed on said legal issues on June 7, 1976. This Court has not yet ruled on said issues. This case has and is moving forward most expeditiously considering the delays which rehabilitation cases necessarily involve considering the rights of a debtor under the Act. The conduct of this case has fully complied with the requirements of Rule 12-43 (d) of the Rules of Bankruptcy Procedure concerning priority to be given to complaints seeking relief from the effects of a stay entered in a Chapter XII proceeding. In view of the evidence presented to this Court as to the value of the real property involved, the extent of the secured debt and the economic condition — past, current and anticipated — this Court deems that no constitutional rights of these creditors have been or are being impermissibly offended by any delay and inconvenience occasioned thus far by these Chapter XII proceedings. See the decision of the United States Court of Appeals for the First Circuit in the Chapter XIII case, *Cheetam v. Universal C.I.T. Credit Corp.*, 390 F.2d 234, 237 (C.A. 1, 1968).

business operation, the Court further concludes that Plaintiffs are not entitled to the relief requested, since Plaintiffs will suffer no irreparable harm through the continuation of the stay injunction in this case. See *In Re: General Stores Corp.*, 47 F.Supp. 350, and *Kaplan v. Anderson,* 256 F.2d 416. In fact, it appears to the Court from the testimony of all parties in this matter, that the Debtor is taking exactly the same steps, albeit in the context of a rehabilitation proceeding, that would be required of the Plaintiffs if they were granted the relief they seek.

Additionally, the Court concludes that there exists a reasonable possibility of reorganization, and the Court is unwilling to release the Debtor's single most important asset to these Plaintiffs while such a possibility continues to exist.

Based upon these cogent equitable reasons, therefore, the Court denies Plaintiffs' request that they be allowed to exercise their power of sale against the Pine Gate project. See *In Re: Yale Express Systems, Inc.,* 370 F.2d 433.

B. SEQUESTRATION OF RENTS

With regard to Plaintiffs' request for an Order sequestering the rents generated by the Pine Gate Apartment complex, the Court also concludes that Plaintiffs are not entitled to this relief based upon the equitable considerations relevant to a rehabilitation proceeding.

In a reorganization situation, the ability of the Court to deal with rents, profits, or income accruing from the Debtor's property is extremely broad, and thus within the discretion of the Court. See *In Re: Philadelphia & Reading Coal & Iron Co.,* 117 F.2d 976. In exercising this discretion, the Court believes that the broad purpose of reorganization is the paramount concern, and the rents and profits accruing to the Debtor's property should not be sequestered and paid over to a creditor unless the Court is satisfied that the retaking of the income, or any part of it, by the creditor, will not prejudice the operation of the business of the Debtor during the reorganization proceeding. *In Re: Philadelphia & Reading Coal & Iron Co., supra.* For an earlier case involving the Frazier-Lemke Act, a farmer relief act preceding the Chandler Act, which act provided for an extension of the period of redemption contrary to the contractual rights of secured creditors, the Supreme Court of the United States held that before payment of the proceeds of a crop to the mortgagee, funds might be withheld to pay the expenses of harvest and cultivation for the next crop year on the theory that such expenditures would ultimately benefit the mortgagee. *Adair v. Bank of America National Trust & Savings Association,* 303 U.S. 350 (1938). Also, see *Wright v. Union Central Life Insurance Co.,* 304 U.S. 502 (1938) and "Restraint and Reimbursement: The Secured Creditor in Reorganization and Arrangement Proceedings" by Patrick A. Murphy in the *Business Lawyer,* Vol. 30, November, 1974, page 25.

The possession of income during the course of a reorganization proceeding is a matter of remedy, and not of right, since such income is, in any event, subject to the necessary operating and administrative expenses of the reorganization estate. *In Re: Philadelphia & Reading Coal & Iron Co., supra.* In this case, the monies being generated by the Pine Gate project are being paid into a fund over which this Court exercises direct supervision and control and in regard to which the Plaintiffs

have the right of review of the expenditures and accounting for same. Moreover, as found by the Court above, the expenditures of these monies are for purposes directly related to the continued operation and maintenance of the Pine Gate project. Not only are these expenses authorized as expenses of administration for which this fund might be charged, but, and perhaps more significantly, these same expenses would have to be incurred by Plaintiffs in the operation of the Pine Gate project if this Court were to grant their request to foreclose on the project.

Since these funds are absolutely essential to the continued operation of the Debtor's property (and therefore the Debtor's business), the Court, in its equitable discretion, believes that Plaintiffs are not entitled at this time to an order sequestering these monies to the exclusive control of Plaintiffs.

C. DEBTOR'S COUNTERCLAIM

Since the evidence presented to the Court compels the findings earlier made herein that the counterclaim asserted by the Debtor against the Plaintiffs is valid, and this Court concludes that the Plaintiffs are liable to the Debtor in the sum of $22,477.82. The Court further concludes that this liability cannot be offset against any amount owing to the Plaintiffs because the agreements between the Plaintiffs and the Debtor limit the right of recovery of the Plaintiffs on their debts to the real property which constitutes their security.

Also, in reaching this conclusion, the Court deems it extremely significant that the proceeding before the Court is a rehabilitation proceeding, rather than a straight bankruptcy. In rehabilitation, the Debtor must continue in operation, and for that reason must be able to use and have available to it all of its current assets. See *Susquehanna Chemical Corp. v. Producers Bank and Trust Company,* 174 F.2d 783. Although a setoff might be allowable and acceptable in a liquidation context in which the purpose was merely to liquidate both the claim and the assets of the bankrupt and distribute the proceeds of said assets, in a reorganization proceeding, the concept of rehabilitation and continuation in operation will not be served by allowing a claimant to deprive a Debtor of its current assets (such as a judgment debt) by setting off a claim which may be altered or compromised in a Plan of Reorganization.

Although setoffs are acknowledged and allowed under Section 68 of the Bankruptcy Act, that section, as well as all other provisions of straight bankruptcy, would only be applicable to a rehabilitation proceeding where it was not inconsistent with the purposes of reorganization. The Court concludes, however, that Section 68 is inconsistent with said provisions to the extent that it would allow a creditor to deprive a Debtor of an asset which it might use in its attempt to reorganize. See *In Re: Yale Express System, Inc., supra.* See also *In Re: Preferred Surfacing, Inc.,* Civil Action No. B75-1287A, USDC, Northern District of Georgia, Order of Judge Hill dated September 25, 197...., affirming the Order of Bankruptcy Judge Norton dated May 12, 1975.

Based upon the findings of fact and conclusions of law stated above, it is

ORDERED that any and all relief requested by Plaintiffs in their Complaint, be, and the same hereby is, denied at this time, and it is

FURTHER ORDERED that Defendant have judgment against Plaintiffs in the sum of $22,477.82, and that Plaintiffs be, and they ~~hereby~~ are, ordered to pay said sum to Defendant forthwith.

SO ORDERED, this 30th day of June, 1976.

WILLIAM L. NORTON, JR.

William L. Norton, Jr.
United States Bankruptcy Judge
United States Bankruptcy Court
United States District Court
Northern District of Georgia
Atlanta Division

APPENDIX I

IN THE UNITED STA ES DISTRICT COURT
FOR THE NORTHERN ISTRICT OF GEORGIA
ATLANT DIVISION

IN THE MATTER OF: PINE GATE ASSOCIATES, LTD., Debtor GREAT NATIONAL LIFE INSURANCE COMPANY, formerly USLIFE LIFE INSURANCE COMPANY OF TEXAS, and ALL AMERICAN LIFE AND CASUALTY COMPANY, Appellants vs. PINE GATE ASSOCIATES, LTD., Appellee	BANKRUPTCY FILE NO. B75-4345A FILED IN CLERK'S OFFICE NOV. 1, 1976 BEN H. CARTER, Clerk By: Deputy Clerk

ORDER

This Chapter XII proceeding is before the court on the appeal of plaintiffs, Great National Life Insurance Co., from the order of the Bankruptcy Court of June 30, 1976, denying the relief asked by plaintiffs (hereinafter appellants) and granting judgment to defendant debtor (hereinafter appellee) on its counterclaim in the amount of $22,477.82.

Appellants insist that their appeal presents three questions for decision by the district court: (1) whether the Bankruptcy Court erred when it failed to modify the automatic stay against foreclosure to allow USLife to exercise the power of sale granted under its security deed from Pine Gate; (2) whether the Bankruptcy Court erred when it found that USLife was not entitled to an order sequestering rents and profits derived from the operation of the Pine Gate apartments; (3) whether the Bankruptcy Court erred when it awarded Pine Gate $22,477.82 on its counterclaim. The court dealt with the first two questions in its order of October 19, 1976, in this case. Appellants insist that "the Bankruptcy Court failed to consider the propriety of a Chapter XII proceeding by a debtor whose sole asset is an apartment project with a maximum value substantially less than the amount of the first mortgage alone where that first mortgage holder is a non-consenting creditor insisting on its rights to full compensation or return of the secured property." Appellants insist that § 461(11) of the Bankruptcy Act, which provides a method for confirming a debtor's plan in the face of opposition to the plan by a class of creditors, cannot be used in this situation. This issue is not before the court at this time but is, rather, pending before the Bankruptcy Court. It would be most inappropriate for this court to consider appellants' arguments concerning the applicability of § 461(11) to the instant case before the Bankruptcy Court has ruled on the matter.

Since the first two issues brought up on appeal have been addressed by the court in its previous order, the only issue remaining is whether the Bankruptcy Court erred in its finding the appellants liable to the appellee on its counterclaim and its further conclusion that a setoff would be injurious to the rehabilitative plan. The Bankruptcy Court found the appellants liable to the appellee for (1) wrongfully refusing to fund the so-called "floorloan," the initial funding of the permanent financing required by the terms of the commitment letter to Pine Gate's predecessor in interest, in order to obtain a restrictive covenant in the deed to secure debt; (2) wrongfully delaying the closing of the "ceiling" portion of the permanent financing. The Bankruptcy Court found that appellee suffered damages in the amount of $22,477.82.

As both parties have pointed out to the court, rule 810 of the Bankruptcy Rules provides, in pertinent part: "The court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge the credibility of the witnesses." Since the court has been shown no evidence of erroneous findings in regard to the counterclaim, the findings of fact as presented by the Bankruptcy Court will not be disturbed.

However, appellants argue that the conclusion of law as to liability is erroneous because under Georgia law all prior inconsistent agreements, written or oral, merged into the deeds and final loan contract. Appellants cite a number of cases applying the Georgia rule of merger. However, the situation in this case has nothing to do with the doctrine of merger because the letter of commitment was a contractual agreement which was breached *before* the final deeds and loan contract were made. Damages flowed from this breach for which the appellee is entitled to compensation. Further, as appellee points out, the consummation of the final deeds and loan contract cannot be considered a novation in that there is no evidence of consideration. Acceptance of the final deeds and loan contract by appellee did not constitute waiver of the right to damages for breach of the letter of commitment.

The question of the setoff of appellants' liability under the counterclaim against the amount of the debt owed appellants by appellee is a more serious question. Section 68 of the Bankruptcy Act provides for the right of setoff in a straight bankruptcy situation. Section 102 of the Bankruptcy Act provides that the general provisions of the Bankruptcy Act apply under Chapter XII "insofar as they are not inconsistent or in conflict" therewith. Courts construing the setoff question in regard to Chapter X rehabilitative proceedings have held that when the loss of the cash represented by the counterclaim would be injurious to the success of the rehabilitative plan, a setoff is not appropriate. *See, e.g., In re Penn Central Transporation Co.*, 486 F.2d 519 (3rd Cir. 1973), *cert. denied*, 415 U.S. 990 (1974); *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783 (3rd Cir. 1949); *Penn Central Transportation Co. v. March Warehouse Corp.*, 356 F. Supp. 567 (S.D. Ind. 1972). The same would certainly be true in a Chapter XII proceeding.

The cases construing the setoff provision of the Bankruptcy Act in a rehabilitative setting refer to the "equities" of the situation. The court is quite aware of the fact that depriving a debtor of the cash represented by the counterclaim might endanger the rehabilitative plan. On the other hand, the appellants, the sole secured

creditors, have not assented to the plan. If the Bankruptcy Court rules that the provisions of § 461(11) are applicable to them, it is likely that they will never realize the full amount of their debt. On the other hand, if the Bankruptcy Court decides that § 461(11) is not applicable in this situation and that full and immediate compensation is due, the rehabilitative plan will necessarily fail. In the latter event, the policy behind not allowing a setoff in a rehabilitative situation would no longer be present. If § 461(11) is found applicable, and the appellants are forced to accept less than full compensation, a refusal to allow a setoff would seem to be inequitable.

Accordingly, the court affirms the order of the Bankruptcy Court in all regards except with respect to the setoff. The court vacates this portion of the Bankruptcy Court's order and remands the question of setoff for further consideration of the Bankruptcy Court after it rules upon the question of application of § 461(11) to the instant case.

IT IS SO ORDERED this 11th day of November, 1976.

/s/ WILLIAM C. O'KELLEY
William C. O'Kelley
United States District Judge

APPENDIX J

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

IN THE MATTER OF: PINE GATE ASSOCIATES, LTD., Debtor	IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII CASE NO. B75-4345A

DEBTOR'S PROPOSED PLAN OF ARRANGEMENT

I. PREAMBLE

Pine Gate Associates, Ltd. is a Georgia limited partnership with offices located at Suite 1806, Gas Light Tower, 235 Peachtree Street, N. E., Atlanta, Georgia. The partnership consists of Mr. David R. Vaughan as the sole general partner and 17 limited partners. The partnership is engaged in the business of owning and operating a 118 unit apartment project located on Beaver Ruin Road in Norcross, Gwinnett County, Georgia.

On December 23, 1975, the partnership filed a petition under Chapter XII of the Bankruptcy Act for an arrangement with its creditors. At the First Meeting of Creditors held on February 10, 1976, the partnership was given until March 29, 1976 in which to file its proposed Plan of Arrangement and this date was subsequently extended by the Court until May 14, 1976. Since the filing of the Chapter XII petition, the partnership has operated its property as a Debtor in Possession.

The partnership's proposed plan of Arrangement as set forth hereinafter will be financed through a re-financing of the existing debt structure on the apartment project of a sale of the apartment project.

A ballot for voting purposes accompanies a copy of this Plan being distributed to each creditor entitled to vote thereon and the Court has established the 27th day of May, 1976, as the date on which the hearing on confirmation will be held upon application for confirmation by the Debtor. A creditor may submit his ballot on or before the hearing on confirmation.

An attempt has been made in the Plan described below to treat the secured and unsecured classes of creditors equitably. Under the proposed Plan, neither class will receive payment in full but each class will receive a substantial payment within a reasonably short period of time. The partnership believes that a failure to confirm a Plan and the inevitable adjudication which would follow would be to the detriment of both classes of creditors.

II. DEBTOR'S PROPOSED PLAN

Pine Gate Associates, Ltd., Debtor in this proceeding, proposes pursuant to Chapter XII of the Bankruptcy Act the following Arrangement with its creditors:

A. **Division of Creditors Into Classes.**

Creditors of the partnership are divided into the following classes:

(1) *Secured Creditors* — There are hereby created four (4) general classes of secured creditors. The division of the secured creditors into general classes is based upon the priority or nature of their respective security interests in the property of the partnership.

The general classes of secured creditors are as follows:

Class 1 — Included in Class 1 are those creditors holding a first mortgage position in regard to the apartment project.

Class 2 — Included in Class 2 are those creditors holding a second mortgage position in regard to the apartment project.

Class 3 — Included in Class 3 are those creditors holding a security position in regard to the real property upon which the apartment project is located only.

Class 4 — Included in Class 4 are those creditors having a security interest in real property owned by the partnership other than the real property on which the apartment project is actually situated.

The creditors falling within the various general classes of secured creditors are shown on Exhibit "A" attached hereto and made a part hereof.

(2) *Unsecured Creditors* — There is hereby created one (1) general class (Class of 5) of unsecured creditors which consists of all creditors of the partnership holding valid claims against the partnership for which there is no security and excluding any claims entitled to priority under the provisions of Chapter XII of the Bankruptcy Act. A listing of the creditors included in Class 5 is attached hereto and made a part hereof as Exhibit "B".

(3) *Creditors Holding Priority Claims* — There is hereby created one class (Class 6) of creditors holding claims against the partnership which are entitled to priority under Section 64 of the Bankruptcy Act.

A listing of the creditors included in Class 6 is attached hereto and made a part hereof as Exhibit "C".

B. **Provisions Modifying or Altering the Rights of Creditors Holding Debts Secured by Real Property of the Partnership.**

(1) Creditors in Class 1.

Not later than six (6) months following the date upon which the order confirming this Plan of Arrangement becomes final, creditors included in Class 1 shall be paid in cash the sum of One Million Two Hundred Thousand Dollars ($1,200,000.00) to be divided among said creditors in the relationship each of said creditors' debt owed to them by the partnership bears to the total debt owed creditors included in Class 1. Said payment shall be in full satisfaction of any and all obligations of the partnership and any general or limited partners thereof to said creditors and, upon said payment, said creditors shall execute releases, cancellations of indebtedness or security deeds and any other documents necessary to extinguish

any claims said creditors may have had against the partnership or the property of the partnership.

(2) Creditors in Class 2.

The creditor included in Class 2 shall be paid not more than six (6) months after the date upon which the order confirming this Plan of Arrangement becomes final seventy-five (75%) percent of the remaining unpaid principal balance on the loan held by said creditor and secured by the apartment project. Said payment shall be in full satisfaction of any and all claims which said creditor may have against the partnership or against the property of the partnership but not against the general partner of the partnership individually. Upon said payment, said creditor shall execute any releases, cancellations of indebtedness and other documents necessary to extinguish any claim said creditor may have against the partnership or the property of the partnership.

(3) Creditors in Class 3.

The creditor in Class 3 shall be issued not later than six (6) months following the date upon which the order confirming this Plan of Arrangement becomes final a promissory note by the partnership in the amount of One Hundred Twenty Thousand Dollars ($120,000.00) and bearing interest at the rate of six (6%) percent per annum with said interest payable on the anniversary date of the note in each year but payable only from the "net profits" from the operation of the apartment project during that year and, to the extent not paid from said "net profits" in any year, accruing to the next year. The principal of said note shall be payable in five (5) equal consecutive annual installments with the first such installment being payable on the thirty-sixth (36th) anniversary date of the note (or on the first (1) anniversary date of the note following the payment in full of the loan or loans secured by a first mortgage on the apartment project) with the other four (4) installments being due on the next four (4) anniversary dates of the note. The payment of the interest, and principal when due, shall be secured by the "net profits" from the operation of the apartment project. "Net profits" as used herein shall mean any monies received by the partnership from the operation of the apartment project after deduction of all debt service and operating expenses including, without limitation, taxes, utilities, appropriate reserves, maintenance, management fees and legal and accounting expenses.

On or before four (4) months after the date of said note, the creditor included in Class 3 shall be entitled, at its option and upon so stating in writing to the partnership, to convert its note in full satisfaction thereof and become a limited partner of the partnership in a new class of limited partners to be created on the terms and conditions set forth in this paragraph. Said new class of limited partners shall be composed of the individual and representative members of the creditor included in Class 3. Said class of limited partners shall be entitled in priority to the rights of any other limited partners of the partnership to receive in cash and/or tax benefits an amount equal to One Hundred Twenty Thousand Dollars ($120,000.00). The priority right of said new class of limited partners to receive said cash and/or tax benefits shall continue from year to year until said new class of limited partners shall have been paid from said cash and/or tax benefits One Hundred Twenty Thousand Dollars ($120,000.00). After said new class of limited

partners has been paid in cash and/or tax benefits said One Hundred Twenty Thousand Dollars ($120,000.00), said additional class of limited partners shall lose its right to priority cash and/or tax benefits in preference over the initial limited partners of the partnership and shall at said point become entitled to share any additional cash and/or tax benefits from the operation of the partnership with the initial limited partners on the basis that said new class of limited partners shall receive twenty nine (29%) percent of any additional cash and/or tax benefits.

Upon the partnership's issuance of its note to said creditor or upon the subsequent issuance of an interest in said partnership to said creditor as above provided, said creditor shall execute any and all releases, cancellations of indebtedness or other documents necessary to extinguish any claims or surrender any interests previously held by said creditor against the partnership, its partners or its property except to the extent preserved by this Plan of Arrangement.

(4) Creditors in Class 4.

Not later than six (6) months after the date upon which the order confirming this Plan of Arrangement becomes final, each creditor included in Class 4 shall receive in cash from the partnership the sum of Two Thousand Dollars ($2,000.00). Upon said payments, each of said creditors shall execute any and all releases, cancellations of indebtedness and other documents necessary to reflect the full satisfaction and extinguishment of any and all claims each of said creditors has or may have had against the partnership, its partners or its property.

C. Provisions Modifying or Altering the Rights of Unsecured Creditors.

(1) Creditors in Class 5.

Each creditor included in Class 5 which does not waive in writing said creditor's entitlement to payment under this Plan of Arrangement prior to the time said payment is due shall receive from the partnership a cash payment not later than six (6) months after the date upon which the order confirming this Plan of Arrangement becomes final an amount equal to fifty (50%) percent of its valid claim against the partnership. Said payment shall be in full satisfaction of any and all claims which said creditor may have or may have had against the partnership, its partners or its property arising out of the operation of the business of the partnership.

(2) Creditors in Class 6.

Each creditor included in Class 6 which does not waive in writing said creditor's entitlement to payment under this Plan of Arrangement prior to the time said payment is due shall receive from the partnership a cash payment not later than six (6) months after the date upon which the order confirming this Plan of Arrangement becomes final an amount equal to its claim against the partnership to the extent said claim is entitled to priority under Section 64 of the Bankruptcy Act. Said payment shall be in complete satisfaction of said priority claim against the partnership, its partners or its property.

D. Debts to be Paid in Cash in Full.

All debts included in Class 6 are to be paid in cash in full within six (6) months of the date upon which the order confirming the Plan of Arrangement becomes final.

E. Creditors Not Affected By the Arrangement and Provisions with Respect to Them.

There are no creditors of the partnership who are not affected by the Arrangement although the creditors included in Class 6 are to be paid in full in cash within six (6) months of the date upon which the order confirming the Plan of Arrangement becomes final.

F. Provisions for Classes of Creditors Which are Affected By and Do Not Accept the Arrangement By the Requisite Vote.

With respect to any class of creditors which is affected by and does not accept the Arrangement by the two-thirds (⅔) majority in amount of the filed and allowed claims required under Rule 12-37 of the Official Rules under Chapter XII of the Bankruptcy Act, adequate protection for the realization by them of the value of their debts against the property dealt with by the Arrangement and affected by such debts shall be provided in the order confirming the Arrangement by one of the methods set forth in Section 461 of the Bankruptcy Act.

G. Provisions for the Rejection of Executory Contracts.

The partnership affirms all executory contracts.

H. Provisions for the Payment of Administrative Expenses and Other Allowances.

All costs and expenses of administration and other allowances which may be approved or made by the Court in this proceeding shall be paid in cash not later than five (5) months after the date upon which the order confirming the Plan of Arrangement becomes final and unless and to the extent that the deposit of the money necessary for such payments shall be waived by the persons entitled to such payments, the same shall be paid into the registry of the Court not more than three (3) months following the date upon which the order confirming the Plan of Arrangement becomes final.

I. Property of the Partnership Not To Be Dealt With Under the Arrangement.

All property of the partnership will be dealt with by the Arrangement.

J. Means for Execution of the Arrangement.

(1) The apartment project owned by the partnership shall either be sold or refinanced within the time permitted in the Plan of Arrangement and the proceeds resulting from said sale or refinancing shall be used to make payments as provided in this Plan of Arrangement. In addition to that cash, the partnership will have on hand certain cash proceeds accumulated from the operation of the property of the partnership since the filing of the Chapter XII petition. That cash will also be used to make the payments provided for in this Plan of Arrangement.

(2) The partnership shall act as the disbursing agent for the payments required under the Plan and the funds in the hands of the partnership shall be in lieu of any deposit required under the provisions of Chapter XII of the Bankruptcy Act except to the extent this Plan of Arrangement specifically provides to the contrary.

K. Miscellaneous Provisions.

(1) Possible transfer of partnership property — To the extent required by the Plan of Arrangement, the partners of the partnership do and shall consent to the transfer of any partnership property required to be transferred by the provisions of this Plan of Arrangement in which they, or any of them, of record or by law, appear to have any interest therein. Each such partner shall execute any document necessary to clear title.

(2) Bar of Creditor claims — Confirmation of this Plan of Arrangement shall act as a bar to any creditor thereafter pursuing any claim it held or alleges to have held against the partnership, the partners thereof or the property of the partnership arising out of the business of the partnership on the date of confirmation of the Plan of Arrangement except to the extent specifically provided to the contrary herein.

DATED this 14th day of May, 1976.

PINE GATE ASSOCIATES, LTD.

By: DAVID R. VAUGHAN
David R. Vaughan,
General Partner

EXHIBIT "A"

CREDITORS FALLING WITHIN CLASSES 1, 2, 3, 4

CLASS 1:
Great National Life Insurance Company
(formerly known as USLIFE Life Insurance Company of Texas)
Harry Hines Boulevard at Mockinbird Lane
P. O. Box 35844
Dallas, Texas 75235

All American Life & Casualty Company
35 East Wacker Drive
Chicago, Illinois 60601

CLASS 2:
National Bank of Georgia
P. O. Box 446
Tucker, Georgia 30084

CLASS 3:
CRC Joint Venture Number 4
% Mr. Guy Rutland, III
2317 Sagamore Hills Drive
Decatur, Georgia 30033

NOTE: The individual and representative members of the Joint Venture are as follows:

Mrs. Jody H. Burnett
2354 Havenridge Drive, N. W.
Atlanta, Georgia 30305

Mr. Lewis F. Hunter, Jr.
P. O. Box 632
Ponte Vedra Beach, Florida 32082

Mr. Guy Rutland, III
2317 Sagamore Hills Drive
Decatur, Georgia 30033

Mr. David R. Vaughan and The First National Bank of Atlanta, co-Trustees under the Will of George M. Vaughan,
First National Bank of Atlanta
% Ivan Millender
Assistant Trust Officer
2 Peachtree Street, N. E.
Atlanta, Georgia 30303

The First National Bank of Atlanta
Trustee for Norrell Southern Corp. Profit Sharing Plan
% Trust Department Real Estate Division
P. O. Box 4148
Atlanta, Georgia 30302

Mr. David D. Machamer, Trustee for Lamont J. Machamer
% Mr. Quinn Machamer
Dynatron Corp.
P. O. Box 20121
Atlanta, Georgia 30325

Dr. George W. Statham
Trustee for Taylor Children
4112 East Ponce de Leon Avenue
Clarkston, Georgia 30021

CLASS 4:
Mr. Dan Faulk
Faulk Development Company
4875 Lower Roswell Road
Marietta, Georgia 30060

Fidelity Capital Corporation
300 Interstate North, N. W.
Atlanta, Georgia

First American Investment Corporation
300 Interstate North, N. W.
Atlanta, Georgia

EXHIBIT "B"

CREDITORS FALLING WITHIN CLASS 5

Atlanta Gas Light Company
89 Annex
Atlanta, Georgia 30389

Atlanta Rotary DeRooting
P. O. Box 36119
Decatur, Georgia 30032

Axtell-Williams & Assoc.
Suite 117
1699 Tullie Circle, N. E.
Freeway Office Park
Atlanta, Georgia 30329

William L. Kizer
Apt. 6F
2455 Beaver Ruin Road
Norcross, Georgia 30071

Marvin F. Poer & Co.
Suite 688
Century Center
2200 Century Parkway, N. E.
Atlanta, Georgia 30345

John F. McMullan, C.P.A.
Suite 1826
400 Colony Square
Atlanta, Georgia 30361

Oxford Chemicals
P. O. Box 80202
Atlanta, Georgia

Patterson Waste & Equipment
3905 White Oak Lane
Lilburn, Georgia 30247

Poolaide Maintenance & Supply
Co., Inc.
6518 Interstate 85
Norcross, Georgia 30071

Print Shop
Colony Square
1175 Peachtree Street, N. E.
Atlanta, Georgia 30361

Southern Bell
P. O. Box 10051
Atlanta, Georgia 30348

Telechem Corp.
P. O. Box 28818
Atlanta, Georgia 30328

Trimble House Corp.
P. O. Box 726
Norcross, Georgia 30071

David R. Vaughan
General Partner
1806 Gas Light Tower
235 Peachtree Street, N. E.
Atlanta, Georgia

Troutman, Sanders, Lockerman &
Ashmore
Candler Building
Atlanta, Georgia 30301

Diahn's Executive Telephone
Answering Service
1312 Spring Street
Smyrna, Georgia 30080

First Quality Exterminating Service
5269 Buford Highway
Atlanta, Georgia 30340

Kem Manufacturing Corp.
2075 Tucker Industrial Road
Tucker, Georgia 30084

The Puritan Chemical Co.
916 Ashby Street
Atlanta, Georgia

EXHIBIT "C"

CREDITORS FALLING WITHIN CLASS 6

City of Norcross
Norcross, Georgia 30071
CRC Joint Venture Number 4
% Mr. Guy Rutland, III
2317 Sagamore Hills Drive
Decatur, Georgia 30033

STATE OF GEORGIA
COUNTY OF FULTON

I, David R. Vaughan, being the sole general partner of PINE GATE ASSOCIATES, LTD., debtor in this proceeding, do make solemn oath that the partnership has authorized the filing of the foregoing Plan of Arrangement and that the statements contained therein are true and correct to the best of my knowledge, information and belief.

DAVID R. VAUGHAN
David R. Vaughan, General Partner

Sworn to and subscribed before
me this 13th day of May, 1976.

LYNN TAYLOE GWATHIN
Notary Public
Notary Public, Georgia, State at Large
My Commission Expires Jan. 28, 1977

APPENDIX K

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF
GEORGIA, ATLANTA DIVISION

IN THE MATTER OF: PINE GATE ASSOCIATES, LTD., Debtor	IN PROCEEDINGS FOR AN ARRANGEMENT UNDER CHAPTER XII CASE NO. B75-4345A RE: Confirmation of Plan: Applicability of § 461(11)(c)

OPINION

I. Introductory Statement

On December 23, 1975, Pine Gate filed a petition for a real property arrangement under the provisions of Chapter XII of the Bankruptcy Act (Sec. 401 et seq. 11 USCA 801 et seq.) and the Bankruptcy Rules of Procedure 12-1 et seq., in this Court, and was permitted to remain in operation of its property as a Debtor in Possession under the applicable provisions of the Bankruptcy Act and Rules.

The Court has before it the question of availability of Section 461(11)(c) of the Bankruptcy Act to the Debtor to deal with a class of non-assenting first mortgage creditors in a one asset Chapter XII case where the Debtor's proposed Real Property Arrangement Plan has been accepted by all classes of creditors except said mortgagee creditors.[1] The issue arises in the context of a Chapter XII proceeding in which the first mortgagee creditors[2] have consistently opposed the Debtor's attempts to formulate and obtain acceptances for a Plan of Arrangement. Instead, the first mortgagee creditors have attempted to foreclose on the property of the Debtor by having the injunction against foreclosures lifted. The Court has previously on June 30, 1976 denied such relief and that matter is now on appeal to the District Court.

At the hearing on confirmation of the Debtor's proposed Arrangement Plan, the Debtor moved to include in the Plan a proposal to utilize the provisions of Sec. 461(11)(c) to provide adequate protection for the first mortgagee creditors by appraising the value of their security and paying them said amount in cash. The first mortgagee creditors contend that Section 461(11)(c) cannot be used to confirm the Plan of Arrangement over their objections unless they are paid

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[1]There is no issue under Sec. 452 or Rule 12-31 as to the proper classification of creditors entitled to vote.

[2]Great National Life Insurance Company (formerly U.S. Life) and All American Life and Casualty Company.

the full amount of their debts. Said creditors and the Debtor have filed Briefs with the Court and, having considered the evidence presented by the parties at the hearing on confirmation and the other pleadings filed in this Chapter XII case which are a part of the record, the Court makes the following findings of fact and conclusions of law:

II. Findings of Fact

Pine Gate Associates, Ltd. (hereinafter called "Pine Gate") is a limited partnership organized and existing under the laws of the State of Georgia. Pine Gate is engaged in the business of owning and operating apartments known as Pine Gate Apartments and located in Gwinnett County, Georgia, near Norcross between U. S. Highway 23 and I-85.

Great National Life Insurance Company (formerly U.S. Life, Life Insurance Company of Texas) and All American Life and Casualty Company (hereinafter referred to as "Class I Creditors") hold first mortgages against the apartment project owned and operated by the Debtor as a result of two Promissory Notes executed by Pine Gate when the creditors in Class I loaned money to the Debtor in 1973 for construction of the apartment project.

Both Promissory Notes above referred to and the Deeds to Secure Debt contain a so-called "exculpatory clause" under which the Debtor, its general partner and generally all persons associated with the Debtor are relieved from any liability on said notes beyond the value of the property and improvements upon which the apartment project is located.

On May 14, 1976, the Debtor filed its proposed Plan of Arrangement which was promptly circulated to creditors and the hearing on confirmation was held on May 27, 1976. The Plan of Arrangement proposed by the Debtor divided the creditors into six classes. One of the classes, that of priority tax claimants, is not affected by the Plan of Arrangement since it is proposed to pay the debts held by creditors in that Class in full. The Plan of Arrangement is essentially a proposed refinancing of the existing debt structure on the project and the payment, upon said refinancing, of almost all of the remaining principal owed the creditors in Class I but none of the accrued interest. Of the five classes of creditors affected by the Arrangement, only the creditors included in Class I failed to approve the Plan of Arrangement by the two-thirds in amount required by the applicable provision of the Bankruptcy Act (Sec. 468) and Rules (See Rule 12-38).

At the hearing on confirmation, the Debtor proposed that the property constituting security for the debts owed the creditors in Class I be appraised under Section 461(11)(c) and said creditors be paid that amount so that the Plan of Arrangement could be confirmed notwithstanding the negative votes of the two creditors included in Class I. The Class I creditors insist that such an approach does not provide them "adequate protection" as required by Section 461(11) for the realization by them of the value of their debts against the property affected by the Arrangement. They insist that Section 461(11)(c) requires that their debts be paid in full or the property surrendered to them upon adjudication or dismissal.

III. Discussion

A review of some of the background of this rehabilitation Chapter XII seems appropriate as orientation to the issues before the Court preparatory to the determination of what Congress intended in § 468 and § 461(11). As described by the Court in *In re Colonial Realty Investment Co.,* [3]

> "The Chandler Act enacted in 1938 effected a general modernization of the Bankruptcy laws. Pub. L. No. 696, 75th Cong., 3d Sess. The most substantial changes wrought by the Chandler Act involve not the liquidation provisions of the existing law, but those dealing with reorganizations, compositions and arrangements, §§ 12, 74 and 77B of the then existing law."[4]

> ". . . Section 77 B had been enacted as an emergency measure four years earlier. Act of June 7, 1934, 48 Stat. 911."[5]

> ". . . Congress sought both to remedy abuses prevalent under existing law, and to provide effective machinery for the rehabilitation of weakened but still viable business enterprises. Chapter XII was enacted principally ' . . . to furnish the same relief to individual debtors as is now available to corporations under Section 77B or under Chapter X of this bill.' " H. R. Rep. No. 1409, 75th Cong. 1st Sess. (1936) at 51.[6]

The drafters of the Chandler Act viewed Chapter XII as a provision which would become increasingly important as the growth of corporate tax problems encouraged non-corporation property ownership, a pattern then prevalent only in Chicago. Weinstein, *The Bankruptcy Law of 1938, a Comparative Analysis,* at 296. But, its popular use was not instant as possibly anticipated. And surely the Congress could not have visualized the geometric increase in use of the unincorporated forms for ownership and development of real property which has occurred since 1938. The popularity of limited partnerships; i.e., syndications, during the past two decades, accentuated because of income tax advantages, has concentrated billions of dollars of real estate in such unincorporated entities.

Dealing with the creditor's argument that Chapter XII differed in scope and power from Chapter X, the court, at footnote 8, p. 158, in the *Colonial* case, *supra,* concluded:

> "The history of the Chandler Act and the context of the parallel provisions [of Chapter X and XII] diminish, in our view, the significance of the difference . . . ."

Yet, Chapter XII is basically more patterned after and akin in procedure and status to Chapter XI. The procedural steps required in a Chapter XII are substantially identical to Chapter XI. Chapter XI affects unsecured and only unsecured creditors generally, while Chapter X has no jurisdictional limitations

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[3] 516 F.2d 154 (1975).

[4] *In re Colonial Realty Investment Co.,* 516 F.2d 154 (1975) p. 157.

[5] *Id.*

[6] *Id.*

as to creditors of all categories.[7] While Chapter XII has its genesis in Chapter XI, it has vestiges of the Chapter X philosophy, especially in its authority to deal effectively with recalcitrant secured creditors. From his study of all the rehabilitation chapters, Professor Nadler stated in summary, that it is a "seeming overlapping of Chapter XII with Chapter XI, and with Chapter XIII and with the . . . old Farmers Relief Act (former § 75, Chapter VIII). Chapter XII, like Chapter XIII, has been cut out of the master pattern of what is Chapter XI,[8] . . . but it is cut to meet the rehabilatory needs of another specialized class of debtors, the 'personal' owner of encumbered real property."[9] It is but "another variation of the same basic theme (i.e., debtor relief) adjusted, however, to the special economic status of the 'personal' owner of encumbered real property."[10] "Chapter XII is a composite of Chapter X (in its treatment of secured claims) and of Chapter XI (in its procedural aspects, as well as its consideration of unsecured debts)".[11]

Although the Chandler Act of 1938 was the creator of Chapter XII, as with Chapters X and XI, the use of Chapter XII has been quite limited and neither creditors, debtors, nor the courts are as familiar with its procedures and possibilities of use as with Chapter X and XI which have been in wider use and in which we have had considerably more judicial interpretations.

Prior to 1975, perhaps a deterrent to the use of Chapter XII was contained in the provisions then applicable, which required a plan of arrangement to accompany the petition upon filing, and that a trustee be appointed immediately. Naturally, the additional costs and loss of control resulting from a trustee is abhorrent to a debtor who desires continued possession and control of the business. However, the recently enacted Bankruptcy Rules, enacted effective August 1975, change both of these requirements. Bankruptcy Rule 12-17 contemplates continued possession by the debtor unless there is some reason for appointment of a trustee. If no trustee is appointed, § 444 provides that the debtor continues in possession of his property and in such status is a trustee for all practical purposes. See Rule 12-17 and *In re Walker*, 93 F.2d 281 (CA 2, 1937). Also, Bankruptcy Rule 12-36 offers the debtor more flexibility now than the restrictive §§ 423 and 534 by providing that the plan may be filed with the petition "or thereafter" at a time as approved by the court. And, § 466 allows a creditor or creditors under certain conditions to file a plan.

However, even prior to the effective date of Bankruptcy Rules 12-17 and 12-36, this court had experienced a dramatic increase in use of Chapter XII as a means for rehabilitation of the substantial number of real estate projects, notably the recently popular limited partnership, in this district which are experiencing

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[7]Nadler, *The Law of Debtor Relief*, (1972), § 585, p. 656.

[8]*Id.*

[9]*Id.* § 584, p. 653.

[10]*Id.* § 585, p. 655.

[11]*Id.*

distressed conditions.[12] With the advent of publicity from news articles[13] extolling the possible advantages of Chapter XII to the distressed real property operator, the volume of Chapter XII filings is not expected to soon abate.

In this case the issues involve the provisions governing possible confirmation of the plan absent approval of all or a majority of the secured creditors.

Section 467 (11 USC § 867), identical to § 361 in Chapter XI, provides for the confirmation if the plan is "unanimously accepted" by all affected creditors.

Absent such unanimity, § 468 provides that the court may still confirm the plan if the arrangement is accepted by two-thirds amount of the proved and allowed claims of all classes of creditors and if the requirements of § 468 and § 472 and § 521 and § 455 are satisfied. The similar § 362(1) of Chapter XI provides that the plan must be confirmed by a majority of creditors in number and amount of the claims proved and allowed.

And, Section 468(1) goes one step further by making provision for the approval of a plan absent the otherwise required two-thirds vote if the plan provides "for payment or protection" as provided under § 461. Section 461 contains the so-called "cram down" provisions of Chapter XII.

Section 461(11) provides that an *arrangement:*

> ". . . [s]hall provide for any class of creditors which is affected by and does not accept the arrangement by the two-thirds majority in amount . . . *adequate protection* for the realization by them of the value of their debts against the property dealt with by the arrangement and affected by such debts, either . . . (a) by transfer or sale, or by retention by the debtor, of such property subject to such debts; or (b) by a sale of such property free of such debts, at not less than a fair upset price, and the transfer of such debts to the proceeds of such sale; or (c) by appraisal and payment in cash of the value of such debts; or (d) by such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection." [Emphasis added]

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[12]In this District, one (1) Chapter XII case was filed from 1938 to March, 1974. From March, 1974 through June, 1976, there have been 35 Chapter XII cases filed in the Northern District of Georgia and approximately 862 Chapter XII cases filed nationally. From the enactment of Chapter XII in 1938 to June 30, 1976, approximately 2374 Chapter XII cases were filed in the United States. Yet, in the year ending June 30, 1976, 525 cases were filed. The Administrative Office of U. S. Courts advises that the following cases were filed in fiscal years 1940 through 1976: 40-149, 41-71, 42-52, 43-22, 44-10, 45-5, 46-1, 47-7, 48-20, 49-17, 50-31, 51-22, 52-21, 53-15, 54-12, 55-19, 56-15, 57-24, 58-23, 59-21, 60-12, 61-31, 62-37, 63-33, 64-47, 65-49, 66-75, 67-68, 68-69, 70-58, 71-120, 72-92, 73-92, 74-172, 75-280, 76-525. Approximately one-third of all the cases which have been filed since the Chandler Act of 1938 have been filed during the past two years, 1975 and 1976 — one-half since 1970 — over 40% during 1974-76.

The dramatic surge of Chapter XII filings in this District and in other bankruptcy courts beginning in 1974 reveals that, while this Chapter lay dormant and little used as a vehicle for debtor rehabilitation from 1938 to 1974, the current depressed economic conditions which have visited many parts of this country, triggered by the tight money and substantial inflation in the construction industry and compounded around 1973 by the oil embargo and resultant inflation of 1973-74, has made Chapter XII a mid-30's, Great Depression, idea whose time has finally come. Due credit should be given for Congressional reforms of over a generation ago for the availability of this convenient vehicle for rehabilitation to partnership realty owners.

[13]E.g.: *Business Week*, Nov. 3, 1975, "Chapter XII Bankruptcy: A Grim Case in Atlanta," pp. 70-71.

Section 461 makes provision for the eventuality of there being a class of creditors who is both "affected" and "non-accepting," and requires that, in such a situation, the arrangement must set forth adequate protection for such creditors. Clause (11) of § 461, therefore, offers the third alternative to the debtor to enjoy the rehabilatory benefits of Chapter XII even though an affected class of creditors has failed or refused to accept the arrangement by the requisite majority of two-thirds. An arrangement can accomplish this result only where it provides that such affected and non-accepting class is "adequately protected" by one of the four methods set forth there. One Chapter XII case[14] has stated that the obvious connotation of § 461(11) is that no arrangement shall be blocked because *one group* of creditors opposes it, provided that they are adequately protected by the arrangement.

Since § 468 makes it possible (as does § 362(1), majority in number and amount) for an insolvent debtor to bind all of his affected creditors without the necessity of obtaining their unanimous consent, the minority dissenters are bound by the majority approvers. But § 468(1) and § 461 go one step further; to permit a debtor to bind a majority of a dissenting class of creditors to the plan.

The aforequoted four statutory methods employed by § 461(11) of Chapter XII for the adequate protection of any dissenting affected class of creditors are identical with those used for the same purpose by Chapter X in § 216(7).

While many of the provisions of Chapter XII and Chapter X are parallel in content and almost identical in thrust in dealing with real property secured creditors, there are differences, and the differences militate in favor of greater liberality of approval of a Chapter XII plan of arrangement than in Chapter X. One difference is that § 141 of Chapter X requires an initial hearing and finding on "good faith" filing while in Chapter XII the petition is filed as a matter of right. Section 412, 11 USC § 812. And, the real estate sought to be arranged in Chapter XII need not be primarily a part of a business as in Chapter X and XI. Section 406 and *In re Bearden*, Case No. B75-2756A, dated December 23, 1975, Bankruptcy Judge Norton, (ND Ga.). And the SEC is less likely to impede the confirmation since, as will be discussed hereinafter (see fn 26 and 27), the 1952 omnibus amendments to the Bankruptcy Act eliminated the "fair and equitable" test from Chapter XII as a prerequisite to confirmation as required by § 221 in Chapter X. This 1952 amendment gives Chapter XII even more attributes of the liberality of confirmation of Chapter XI and XIII. The 1952 amendment demonstrates that even the "cram down" provisions of § 461 are to be confirmed more readily for the "personal" debtors in Chapter XII cases than the same provisions of § 216 for corporate debtors in Chapter X cases.[15]

[14] *In re Herweg*, 119 F.2d 941 (CA 7, 1941). See also fn 29.

[15] As observed by a Chapter XII commentator, Robert K. Lifton, *The Business Lawyer*, "Real Estate in Trouble; Lender's Remedies Need an Overhaul", p. 1927 at p. 1955.

"As a result of these differences, the debtor in a Chapter XII has substantially greater leverage to push through a plan of arrangement than in a Chapter X. This leverage seems to be considerably buttressed by the elimination of the 'fair and equitable' test from Chapter XII of the 1952 Amendment to the Act."

"Prior to 1952 the 'fair and equitable' test contained in Chapter X was also required for confirmation of a Chapter XII plan by § 472(3). The 1952 Amendments to the Act, (1952 Chandler Act Amendments, Pub. L. No. 456, 66 Stat. 579, 11 USC § 1-1086 (1970)), however, deleted the 'fair and equitable' test from § 472, leaving us the only standards for confirmation under § 472 that 'the arrangement is for the best interest of the creditors and is feasible' . . . ."

The committee reports do not offer a lengthy explanation for the reasons for this deletion from Chapter XII. The 1952 Amendment also eliminated the "fair and equitable" language from Chapters XI and XIII. The report dealt primarily with the reference Chapters XI and XIII and stated "nor is it practical or realistic to apply the rule in a proceeding under Chapter XI, XII or XIII . . . ." See fn 26 and 27, herein.

To make sure that the absolute priority rule as applied to corporate reorganization would not work its way into Chapter XII arrangement proceedings, § 472 was also amended by adding a paragraph which specifically provides that "confirmation of an arrangement shall not be refused solely because an interest of a debtor would be preserved under the arrangement." Congress obviously deemed a finding that the plan is "for the best interest of creditors" as sufficient protection for creditors in light of the philosophy of Chapters XI and XII to expedite "single" compositions. See *SEC* v. *American Trailer Rentals Co.*, 379 US 594 (1965).

Whatever differences in Chapters X, XI, XII and XIII exist, the primary socio-economic purpose of each chapter to effect rehabilitation of the debtor remains consistently common.

The *Colonial* court, supra, at p. 158 stated:

> "We deem the language and history we have described persuasive indicia of Congress' intent to equip courts acting under Chapters X and XII with similar power with which to execute similar missions . . . The purpose of Chapter X and XII is to restore, not to dismantle, the economically distressed debtor."

And at page 160:

> "The policy of Chapter XII is rooted in society's interest in substituting arrangement for liquidation where possible and confers powers on the court to insure a fair chance to realize a viable arrangement."

It is in this background that the Debtor here seeks to confirm the plan over the dissenting vote of the Class I secured creditors by applying the provisions of § 461(11)(c) and satisfying this debt by paying in cash the appraised value of the debt to said class of creditors.

The Class I creditors in this case construe the emphasized language quoted above from Section 461 to mean the debts under the secured agreement must be paid in full for that section to be utilized as an alternative to assent to the Plan by a class of creditors. The Court cannot agree.

(a) What does § 461(11)(c) say?

It authorizes the debtor to include in the real property arrangement a plan to continue to hold and keep the property to use in the debtor's business enterprise under certain conditions; i.e., provided the plan offers "adequate protection" to the nonassenting secured creditor so that, upon the loss of the security and extinguishment of the debt, that creditor will realize the value of its debt by:

(1) Appraisal of the value of the debt;

(2) Payment in cash of the value of the debt.

Clearly, the so-called "cram down"[16] provisions of § 461(11) and (12) allow several alternatives for utilization by Chapter XII debtors to deal with and satisfy the debt of a class of nonassenting secured creditors.

In their brief, the Class I creditors cite *Collier on Bankruptcy* to support their contention that the utilization of the Bankruptcy Act necessarily presumes that first priority mortgagees would be paid in full. 9 *Collier on Bankruptcy* (14th Ed.) § 8.12 and § 9.03. Admittedly, there are some comments in Professor Collier's Chapter XII treatise which seem to support that position. Such argument of creditor and *Collier* seem to be that § 461(11) just does not mean what it says. With all deference to *Collier on Bankruptcy*, the Court cannot agree with that construction in the circumstances of this case.

Despite the construction of the Class I creditors and perhaps *Collier*, the inclusion of the subsection (c) in § 461(11) in the Chandler Act was not without prior mature consideration and rationale by the Congress over a period of years prior to 1938.

Without question, should the secured creditor reclaim the property in this Chapter XII proceeding which Congress has authorized; i.e., "by transfer . . . of such property subject to such debts . . ." under subsection (a) of § 461(11), or by sale free of debts as in subsection (b), it would recover the value of its security and its debt would be extinguished. Creditors traditionally argue that if sold through the court as authorized under § 461(11)(b) (which presumably would be close upon the confirmation of the arrangement as in a forced sale rather than in a generally more reasonable period of negotiation), or by foreclosure forced sale outside the court, it is appropriate because the debtor has the option to bid against the secured creditor and others. Yet, as a practical matter, the debtor has no such option. For, only a sale in which a willing buyer and a willing seller negotiate, without the enforced conditions of a sale required within a limited time period or other compulsion, can produce the real value of the property in debtor reorganization.[17] Congress had already recognized prior to enactment of the Chandler Act in 1938, which conceived Chapter XII as a remedy for a particular class of debtors, that such procedure of forced liquidation sale is not, in practice, satisfactory in the determination of value. Moreover, Congress had recognized that sale or release of the property is generally inapplicable or inappropriate to the circumstances of desired reorganization.[18]

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[16]"Cram down" is a term used by some bankruptcy lawyers and bankruptcy commentators to describe the application of § 461 under Chapter XII and § 216 under Chapter X of the Act upon a dissenting class of creditors where the proposed plan failed to receive approval of the requisite majority. The Court has found no judicial or other authoritative definition or discussion of the term or, indeed, few articles which discuss the term oft used by lawyers. Nevertheless, it is a self-evident, valid term of immediate understanding, perhaps requiring no explanation. It creates an instant correct connotation of the involuntary administration of bad medicine upon a recalcitrant victim, the secured creditor who opposes the effects of the reorganization proceedings in the Bankruptcy Court.

[17]*Collier on Bankruptcy*, Art. X, § 10.13, pp. 471-74, fn 19 (14th Ed.) and fn 20.

[18]There "is nothing unjust in substituting some other valuation device in place of a sale, where as a practical matter the right to bid at a sale is nearly valueless." *Collier on Bankruptcy*, Ch. X, § 10.16, p. 488, fn 31 (14th Ed.).

The inadequacy and impracticability of subsections (a) and (b) of § 461(11), under which the real property may be sold or the secured creditor may reclaim the property, as a means of reorganization of the business enterprise (because generally retention of the real property is absolutely essential to the reorganization effort), furnished sufficient reason to Congress of the need for inclusion of § 461(11)(c) in Chapter XII. Subsection (c) was not new when included in Chapter X, § 216(7), and Chapter XII, § 461(11), in the Chandler Act of 1938. The same appraisal device had been previously included in (b)(5)(c) of Section 77B in 1933[19] (the Corporate Reorganization Act of 1933), the predecessor of § 216(7)(c) of Chapter X of the Chandler Act, and had been tested in the Frazier-Lemke Act as Section 75(s),[20] enacted in 1935.

The appraisal device had its genesis in an equity receivership case prior to enactment in § 77B in 1933:

> "[T]he appraisal device was a desirable alternative which would avoid delay and expense and protect the minority at least as adequately as would an actual sale." *Collier, supra*, § 10.16, p. 484, fn 13.

Subparagraph (c) of § 461(11) was, therefore, included by Congress in Chapter XII to provide the alternative of appraisal as determining value, and the payment of the appraised value in cash as adequate protection to the creditor in satisfaction of the debt.

Clause (c) of § 461(11) offers debtors the advantage of a means, at least, other than sale or return of the property, of dealing successfully with a recalcitrant class of creditors who are blocking a reorganization of a financially distressed debtor in the Bankruptcy Court. Yet, obviously, (c) has the limitation inherent in the

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[19]*Collier, supra*, § 10.16, p. 483. Section 77B of the Bankruptcy Act (11 USCA § 207) (Supp. 1937), (the predecessor of Chapter X in the Chandler Act), eliminated the necessity of the judicial sale, which had been crticized as a useless and merely formal part of the prior equity receivership procedure, and authorized confirmation of a plan which has been found by the court to be fair and equitable even without the consent of two-thirds of a class of creditors on certain conditions; i.e., the same four subsections as are now in § 461(11). Also, see *The Yale Law Journal*, Vol. 46, 116, "Provisions for Non-assenting Classes of Creditors in Bankruptcy Reorganizations."

> "It may be contended that methods (a) and (b) provided in subsection (b)(5) [§ 77B, enacted in 1933; (b)(5) was the same as present § 216(7) and § 461(11)] furnish techniques adequate to deal with recalcitrant creditors. But sale or retention of the property subject to liens under (a) would be of no service to a [business entity] in need of having its debt scaled down. And sale of the property at a fair upset price under (b) involves a return to the expensive formality of a judicial sale. Appraisal has several practical advantages over upset price as a means of measuring creditors' claims, from the point of view of both the creditor and of the debtor. Subsection (b)(5)(c) seems definitely to add to the economy and effectiveness of the reorganization process and it is worth saving, if the Constitution and the Courts will permit." [The writer went on to reason from decisions and to correctly predict its constitutional approval by the courts.] 46 *The Yale Law Journal*, 116, 119 (19....), *supra*.

[20]"[T]he Act must be liberally construed to give the debtor the full measure of the relief afforded by Congress [cites], lest its benefits be frittered away by narrow formalistic interpretations which disregard the spirit and letter of the Act."

"Equal protection for debtor and creditor alike can be afforded only by holding that the debtor's request for redemption pursuant to the procedure prescribed on the first proviso of 75(s)(3) [i.e., appraisal and payment of appraisal value] cannot be defeated by a request of a secured creditor for a public sale under the second *proviso* . . . . Under our construction . . . the debtor will be given the benefit of the express mandate of the Act." *Wright* v. *Union Central Life Insurance Company*, 311 US 273, 85 L ed 184, 61 S. Ct. 196 (1940).

difficulty in raising cash with which to pay off the nonassenting class of creditors. Aside from the availability of (c), the experience and observation of this Court has been that the debtor cannot generally come up with the cash to implement such a plan. Hence, as a practical matter, the difficulty factor is quite large upon the debtor to provide in cash the value of the debt under this alternative.

The multiple alternative actions allowed in § 461(11) were deemed by Congress to offer "adequate protection" to dissenting secured creditors. Surely, Congress considered the appraisal action permitted in § 461(11)(c) to be the "indubitable equivalence"[21] of the return of the property as permitted in § 461(11)(a).

If the transfer of the property to the creditor under § 461(11)(a), or as authorized by the loan agreements hereunder consideration in which the debtor and partners are exculpated from liability for the debt, acts to fully extinguish the debt, the value of the debt must be the value of the real property. Hence, if the creditor in lieu of the return of the property receives cash in the appraised value of that property, the creditor receives the "value of the debt" and the creditor is adequately protected as contemplated by § 461;[22] and the plan can be confirmed without the consent of said creditor.[23]

Congress did not equivocate. It clearly intended to say again in § 461(11)(c) that an arrangement for the payment of cash equal to the appraised value of the debt can be confirmed over the objection of a class of dissenting secured creditors.

(b) **What does Section 461(11) mean?**

What does appraisal of the "value of their debts" mean? Appraisal of what? What is the "value of the debt"?

Here, the creditors deem the value of the real property apartment project to be less than the debt and offered evidence to that effect in the trial held on the creditors' complaint to allow foreclosure. What, then, is the "value of the debt". The debt with principal and accumulated interest and charges ($1,454,421.14) exceed the original amount of the loan (i.e., $1,380,000.00) as of the date of the hearing on the creditors' complaint to foreclose.

The provisions of § 461(11) indicate that the creditors must receive "adequate protection for the realization by them of the value of their debts." The Section does not say they are entitled to the amount of their debts. This is true not only because of the wording of the statute but it would be unreasonable to contend otherwise. Clearly, the property which is security for the debts owed the Class I creditors cannot result in those creditors being given greater protection than

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[21]See fn 53. *Collier on Bankruptcy* (14th Ed., Vol. 6A), § 10.17, Art. X, p. 409 ff. for discussion of § 216(7) of Chapter X, which is the Chapter X equivalent and almost identical to § 461(11).

[22]*Collier on Bankruptcy*, Vol. 6A, Art. X, § 10.17, p. 492, fn 12 and 13.

[23]See also *Country Life Apartments, Inc. v. Buckley*, 145 F.2d 935, (CA 2, 1944), where Judge Charles E. Clark stated: "Under Bankruptcy Act § 179, no acceptance need be obtained from a class of creditors or stockholders for whom payment or protection has been provided as prescribed in § 216 (7, 8) . . . ." "Since the nonassenting creditors were thus adequately protected under the trustee's plan, their assent did not constitute a necessary prerequisite to confirmation." *Collier, supra*, Art. X, § 10.15, pp. 482-83.

the value of the security. As a hypothetical example, if the security is worth $100,000 fairly valued, it is absurd to say that Section 461(11)(c) requires payment of $200,000 because the debt is in that amount. To arrive at such a result, one would have to contend that the property is worth more than the property is worth.

When the loan in question was made in 1973, the value of the debt; i.e., the value of the note, was deemed by the borrower and the lender to be probably less than, surely no greater than, the appraised value of the real property project upon completion. By specific provision in the loan agreements, the borrower and partners were specifically exculpated from liability for any part of the debt and the first lien on the real property stood alone as security for the loan.

As a result of those provisions, the Class I creditors have contractually limited themselves to looking to the value of their security to satisfy their debts. They may not look to other assets of the debtor partnership or any of its partners.

Both the creditors and the borrower apparently felt that the property would stand good for the promissory notes, that the loan was adequately protected by the value of the property without any additional collateral in the form of other property or personal pledge from any of the principals of the debtor partnership. Without such exculpation agreement, under Georgia law, the general partners would likewise stand liable for the partnership debts and, to the extent of the assets of the general partner, the secured creditor would have had additional security to this debt.[24] Without the exculpation clause, presumably the note would have had a value in excess of the value of the real property. The real property being the only security here, however, the value of the property is the value of the debt.

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[24]Parenthetically, it seems worth noting, at the risk of the evil of dicta, that the question of liability of a general partner for partnership debts in a Chapter XII partnership case, brings into consideration some serious matters as has been presented in other Chapter XII cases in this Court.

Section 16 of the Bankruptcy Act, generally held applicable to a reorganization proceeding, provides that the liability of co-debtors, which term includes both primary debtors and those who have secondary liability such as endorsers, guarantors and general partners, shall not be altered by the discharge of a bankrupt co-debtor. There are obvious arguments that the discharge of the debts of the partnership accrues only to the debtor and its side of the debt, and not to the liability of the co-debtor who is not a co-petitioner before the court in the Chapter XII proceeding. The court lacks the authority to require a general partner to become an involuntary co-petitioner with the partnership. And, certainly, the discharge granted to the debtor cannot apply to the debts of an individual other than a petitioner.

And, there are some authority that nonassenting creditors may proceed for collection of the deficiency against the co-debtor, should the reorganization plan fail to pay or satisfy the entire debt. See cases cited in fn 2 and fn 9, *In re Helmwood Apartments*, Case No. B75-1764A, Northern District of Georgia, Bankruptcy Judge Norton, May 26, 1976. Yet, the confirmation and consummation of a reorganization, composition or extension plan so providing, and approved without objections, will extinguish all of that debt. See *In re Lane*, 125 Fed. 772, *Cumberland Glass Mfg. Co. v. DeWitt*, 237 US 447, *Francis v. McNeal*, 228 US 695, *Abbot v. Anderson, et al.*, 106 N.E. 782, *Myers v. International Trust Co.*, 273 US 380, and *Nashville Saddlery Co. v. Green, et al.*, 89 So. 816. Such extinguishment of the debt is grounded upon a contractual agreement between the affected creditors and the debtor related to the action of accepting the plan, rather than by any operation of bankruptcy law.

Aside from such decision authority which recognizes the separation of the entities of the co-debtor and Chapter X or XI debtors, in the view of this Court, when a Chapter XII petition has been filed by a partnership, the creditors should be enjoined from proceeding against the co-debtor general partner for collection for that debt scheduled in the debtor's petition until the Chapter XII debtor has been given the opportunity to present a plan of arrangement to the

(c) Are only Class I creditors entitled to vote, where their debt exceeds the value of the security?

Here, the Class I secured creditors do not want their property rights altered or modified as contemplated in Chapter XII under § 406(1) and object to the Arrangement. They contend that since the dollar amount of the debt exceeds the value of the property securing said debt that *only they are entitled to vote* upon the Plan of Arrangement of the Debtor (which they have rejected), and, finally, that in the face of such objection, they cannot be dealt with under the provisions of § 461(11)(c).

To support the rather novel proposition that only they are entitled to vote upon the Plan of Arrangement, the Class I creditors cite the case of *In re Hamburger*,

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court and creditors. *Helmwood, supra,* p. 18-20. The reason is that in the absence of an exculpatory cause, the financial interests of the debtor partnership and its general partners are so mutual and interconnected as to have a merged and unitary status in the Chapter XII proceeding in relation to the common creditors and the common objective to obtain satisfaction of the partnership debts. Such oneness erases the normally existing individuality and separability of said two entities. Such close identification of financial interests generally entitles the individual general partner or guarantor to the protection of an ancilliary injunction from collection proceedings by the common creditors of the debtor. *Helmwood, supra,* p. 18. Equity requires, however, as a protection to the creditor who is enjoined from proceeding against the co-debtor in such circumstances, that said guarantor or general partner likewise be restrained during the period of the formulation of the debtor's plan from any improper dissipation or diminution of his individual assets to the detriment of the Chapter XII creditors. *Helmwood, supra,* p. 24-25.

Although there are distinctions in each, the general purpose of Chapter XII, and of Chapter X, XI and XIII, is to give the debtor pause to marshal within the Bankruptcy Court all of the liabilities, assets and available resources of the debtor to formulate a plan which can be confirmed to satisfy the total debts in accordance to the priorities of said debts. In marshaling the assets of a Chapter XII partnership debtor, a creditor may have additional security for its debt beyond the control or availability of the debtor; that is, the security of the liability of the general partner or guarantor which has not been exculpated from the partnership debt. Hence, should a feasible plan offer less than payment of the entire secured debt and should the secured creditor class fail to assent by a two-thirds vote under § 468, the plan will fail unless the debtor can enforce a provision of § 461(11) or (12) upon the nonassenting class of creditors.

Section 461(11)(c) permits the nonassenting class of creditors to be paid in cash, not necessarily the whole debt, but the appraised "value of the debt" in satisfaction thereof. It would seem that the value of the secured real property and, in the absence of exculpation, the additional appraised value of the general partner's or guarantor's liability would constitute the "value of the debt". The appraisal of the "value of the debt" by the Bankruptcy Court would, therefore, also include the value of the assets of the guarantor or general partner available to pay the deficiency of said partnership debt. Failure to appraise and include the value of the co-debtors' liabilities to determine the total value of the debtor's debt under § 461(11)(c) would not provide "adequate protection" and complete compensation to the creditor of the value of the debt; while inclusion of the value of the co-debtors' liabilities and payment of said total value to the dissenting creditor would provide the adequate protection and complete compensation required under § 461 and the due process clause. While the distinction between individual partnership debts under § 5 is a matter of substance (*Schall v. Camors,* 251 US 239 (1920), and the personal liability of the general partner for the debts of the partnership is distinguishable from the personal liability arising from the partners individual debts (*Rochelle v. U.S.,* 521 F.2d. 844 (CA 5, 1975); *In re Jack Montgomery,* 2 Bankruptcy Court Decisions 425, ... F.2d ..... (CA 9, 1976)), the general partner cannot have his cake and eat it too. Hence, if the general partner is to be protected by an injunction from proceeding outside the Bankruptcy Court to enforce the debt, said general partner or guarantor should submit to the authority of the reorganization court for that purpose in order to so properly apply the appraisal provisions of § 461(11)(c). If the general partners' assets are considered in appraising the "value of the debts" under § 461(11)(c) and the creditor receives that value, the purpose of the Act to reach an equitable and just accord with the debts due the creditors seems satisfied. The primary debt liability of the debtor and the flip-side individual liability of such co-debtor, would both be satisfied by the plan. All aspects of that debt would have been satisfied by confirmation and consummation of the Chapter XII arrangement. And, the creditor would not

117 F.2d 932 (CA 6, 1941). That case involved primarily the question of whether consent of a debtor was required, or participation by a debtor insured, where the sale value of the debtor's property was much less than the indebtedness. In ruling that the provisions of Chapter XII as it then existed did not require such a result, the Court of Appeals in that case, applying the so-called "absolute priority rule" applicable to Chapter X cases,[25] concluded that since other creditors and the debtors in that case had no equity in the hotel property in question, they had no place in the proceedings.

While the Court considers the issue before the United States Court of Appeals for the Sixth Circuit in that case different from the one involved in the present case, the Court deems it significant to note that subsequent to the *Hamburger* case, and many other cases cited and relied upon by the secured creditor, Congress amended Chapter XII of the Bankruptcy Act to eliminate the so-called "absolute priority rule" upon which the *Hamburger* case was based. Specifically, Congress amended subdivision (a) of § 472 of the Bankruptcy Act (11 USC § 872), which had provided, in pertinent part, that the Court shall confirm an arrangement if "it is fair and equitable, and is feasible", and substituted instead, that the court shall confirm a plan "if it is for the best interest of creditors and is feasible."

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be able to proceed against the general partner or guarantor outside the Bankruptcy Court for any part of that debt which has been so dealt with and satisfied under § 461(11)(c) in the confirmed and completed plan. Yet, the co-debtor is not the debtor petitioner. No notice of such appraisal is required to the creditors of the co-debtor. The co-debtor is not before the court; and no judgment or liability would be imposed by the plan or this court upon that partner in this proceeding; hence, no discharge could be granted to such co-debtor. It is merely his liability and his assets which are being additionally appraised to ascertain the correct value of the debt of the debtor. It is the debtor which will be required to satisfy that combined appraisal; not the general partner his part thereof.

It is argued that if it were otherwise, that is, if the unsecured creditors, and the other secured creditors who may not have their debts additionally secured by the liability of the general partner or guarantor, plus the Bankruptcy Court, must all wait until the secured creditor can proceed for collection of all or some part of its debt against the general partner or guarantor, the formulation and presentation of the plan will be delayed, the proceeding would be frustrated and the rehabilitation purpose of Chapter XII will be defeated.

Should the general partner in such a situation fail to submit to the authority or jurisdiction of the court to allow completion of the aforeoutlined appraisal process under § 461(11)(c), sought by the partnership, the true value of the debtor's debt probably cannot be determined. And such failure and refusal would require the court to consider a dismissal of the co-debtor protective restraint and/or the partnership petition. The requirement of the scheduling of general partner co-debtor individual assets and the possibility of the application of such appraisal procedures seems to have resulted in more caution among guarantors and unexculpated general partners toward opting for Chapter XII relief and relief under subsection (c) of § 461(11). These gratuitous comments concerning a few of the more obvious problems resulting from a partnership petition which attempts to apply the cram down provisions are made to illustrate that an exculpation agreement relieving general partners considerably reduces the problems otherwise possible.

Of course, in the case sub judice, with an exculpation of the general partner, such problems are not presented for decision; and the problems here decided are much simpler.

[25]See *Northern Pacific Railway Company v. Boyd,* 288 US 482 (1913), and *Case v. Los Angeles Lumber Products Company, Ltd.,* 208 US 106 (1939), which, when taken together, establish that the requirements of § 221(2) of the Bankruptcy Act that a plan must be "fair and equitable" and "feasible" in order to be confirmed are words of art which mean that each class of creditors, beginning with the most senior and working down to the most junior class, must first receive full compensation for each class's claim, assuming the reorganization matures liquidation values of those claims, before the next class properly participate in the reorganized corporation. See Robert L. Lifton, "Real Estate in Trouble; Lender's Remedies Need an Overhaul", *The Business Lawyer,* Vol. 31, July, 1976, pp. 1942, et seq.

Additionally, Congress added a paragraph which states: "Confirmation of a plan shall not be refused solely because the interest of a debtor will be preserved under the plan."[26] Both the fact of this amendment itself, and the legislative history of this amendment clearly establishes the Congressional intent to allow a troubled debtor in a Chapter XII proceeding to propose and implement a plan of arrangement in spite of its inability to pay all its creditors in full.[27] This amendment and the legislative history clearly refutes any continued validity of the *Hamburger* case. See fn. 15 and p. 10, 11. The statutory rule of "fair and equitable", enunciated by the courts in railroad reorganization and Chapter X cases as the "absolute priority" rule, is not applicable to Chapter XII cases.

In addition to this Congressional mandate, the Rules of Bankruptcy Procedure applicable to cases under Chapter XII, effective August 1, 1975, point inescapably to the conclusion that unsecured creditors may vote on a plan of arrangement in a Chapter XII proceeding even if the value of security for secured creditors is less than the amount of the debts to those secured creditors. For example, consider Bankruptcy Rule 12-31, which provides as follows:

"(a) *Classification of Claims.* For the purpose of the Plan and its acceptance, the Court may fix, after hearing on such notice as it may direct, the division of creditors into classes according to the nature of their respective claims."

"(b) *Valuation of Security.* For the purpose of classification under subdivision (a) of this Rule, of claims which may be secured in whole or in part, the court shall, if necessary, on application of any party in interest, hold a hearing on such notice as the court may direct, to determine the value of the security interest and allow the claim as unsecured to the extent it is enforceable for any excess of the claim over such value."

The language quoted clearly envisions the right of unsecured creditors to vote on a plan of arrangement even where the value of the real property of the debtor is less than the secured indebtedness on it. In the present case, of course, the Class I Creditors are not entitled to vote as unsecured creditors notwithstanding the value of their security, because they have contractually limited their claim to the value of the security. They are not unsecured creditors for the part of the debt which

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[26]Pub. L. 456, 82nd Cong. 2nd Sess., July 17, 1952 U.S. Cong. & Admin. News, 82nd Cong., 2nd Sess., 1952, Vol. I, p. 419.

[27]The Congressional history of this amendment provides, in pertinent part as follows: "These sections [including § 472(a) of the Bankruptcy Act] presently require a finding that a proposed plan under Chapters XI, XII and XIII shall be 'fair and equitable'. In fact, however, *the fair and equitable rule*, as interpreted in *Northern Pacific Railway Company v. Boyd*, 228 US 482, 33 S. Ct. 554, 57 L ed 931 (1913), and *Case v. Los Angeles Lumber Products Company, Ltd.*, 308 US 106, 41 Am. Br. R. N. S. 110, 60 S. Ct. 1, 84 L ed 110 (1939), *cannot be realistically applied, in a Chapter XII, or XIII proceeding. Were it so applied, no individual debtor* and, under Chapter XI, no corporate debtor where the stock ownership is substantially identical with management *could effectuate an arrangement except by payment of the debts of all creditors in full.*

"Chapter XI has replaced the old composition procedure under former § 12 of the Bankruptcy Act, where the fair and equitable rule did not apply. *Nor is it practicable nor realistic to apply the rule in a proceeding under Chapter XI, XII, or XIII.*

"The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the *Boyd* and *Los Angeles* cases shall not be operative under those three Chapters . . . ." *U.S. Cong. & Admin. News*, 82 Cong., 2nd Sess., 1952, Vol. II, pp. 1981, 1982. [Emphasis added.]

exceeds the value of the property. The property is the full and only security for the debt by contract between the parties to the loan.

(d) **Is § 461 applicable to deal with a dissenting class of secured creditors whose debts exceed the value of the security?**

In this context, the Class I creditors, who have voted to reject the Plan of Arrangement proposed by the Debtor, although all other Classes voting thereon have accepted it, argue that they cannot be dealt with as contemplated under the provisions of Section 461(11)(c). They argue and cite vague comments from Collier on Bankruptcy that Section 461(11) cannot apply to an objecting secured creditor holding more than two-thirds of the vote of that class. The effect of such arguments would be that § 461 could never apply to a single asset real estate project, and that a single asset real estate project could never have a Chapter XII arrangement confirmed over the objection of the single first mortgage holder. The secured creditor could always thwart reorganization efforts. Under such an interpretation, § 461 would be meaningless. As stated in (a) and (b) heretofore, such does not seem to be the intent of Congress in enacting Chapter XII and Chapter X and the prior statutes which originated the concept of § 461(11) and § 216(7). Nowhere in Chapter XII is there any exclusion of the benefits of Chapter XII to a debtor having only one secured creditor. The history of the creation of Chapter XII, which was to provide a remedy to property owners to avoid foreclosure under distressed economic conditions, indicates otherwise. It seems to be the clear intent of Chapter XII and § 461 that the contract rights of a secured creditor in property of which a debtor is the legal or equitable owner may be modified or altered even without the consent of such secured creditor so long as the secured creditor receives adequate protection under § 461 to realize the value of its lien.[28] Retention of the property is the statutory scheme of 461(11)(c) and adequate *protection*, rather than consent, of the secured creditor is its keystone.[29] This Court sees no legislative authority which suggests a holding that § 461(11) and (12) apply only to real property debtors having more than one secured creditor.[30] And the legislative history surrounding the removal of the "fair and equitable" rule from Chapter XII and the recent enactment (i.e. 1975) of Bankruptcy Rule 12-31 clearly points to the availability of Chapter XII in a case such as this.[31]

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[28]See fn 50. 52. 53.

[29]Although "Chapter XII contemplates the execution of an arrangement satisfactory to the majority of creditors of each class or of the group of classes affected thereby" . . . the obvious connotation . . . of the language of § 461 is that . . . no arrangement shall be blocked because one group of creditors opposes it, provided they are adequately protected by the arrangement." "[§ 461] goes one step further . . . than old § 77(b) 11 USC § 207 [which provided that a plan of reorganization was not to be thwarted by dissenters where a majority approved] by providing that any class of creditors not accepting the arrangement shall be taken care of in the manner described, thereby enabling the parties to proceed with the arrangement." *In re Herweg*, 119 F.2d 941, [1, 2] at 943. (CA 7, 1941)

Obviously Congress understood that, from the standpoint of the reorganizer, some such provision as § 461(11) was essential, for otherwise 34% of any small class of creditors might block a reorganization to which substantially all the other creditors had assented. See Swain, "Corporate Reorganization under the Federal Bankruptcy Power," (1933), 19 *Va L. Rev.*, 317, 330.

[30]See fn 29.

[31]See fn 15, 20, 26, 27 and 40.

Although the secured creditors object to any alteration of their contractual rights by this Chapter XII proceeding, they do not specifically rely on such argument to support this position, nor does this Court believe that such reliance would be well-founded.[32] Instead, the secured creditors contend that where first priority secured creditors vote against a Chapter XII plan of arrangement, § 461(11)(c) may not be used as an alternative to the acceptance of the plan of arrangement, and point to two cases which they contend support this position.[33] Being extremely few filings in number in comparison to Chapter X and Chapter XI cases, there have been only a few published decisions[34] by the courts in Chapter XII cases. And the Court has found an even smaller number of published decisions dealing with the application of § 461.[35]

Section 461(11) and (12) contain the so-called "cram down" provisions providing a means to a Chapter XII debtor to overcome the non acceptance of the plan under § 468 by the requisite two-thirds majority of any class of secured creditors holding liens on the real property which is the subject of the real property arrangement. Section 216(7) of Chapter X is almost identical to § 461(11).[36] The more numerous Chapter X decisions under § 216 should be helpful and authoritative in construing the application of § 461 here, but again, the application of the "cram down" in Chapter X under § 216(7) is also rare and the decisions meager.[37] The Court has reviewed the *Meyer* case and the *Herweg* case cited by the Class I creditors, and deems it sufficient to point out that those cases are inapplicable to the situation in this case since they involved Chapter XII proceedings in which *all* of the creditors of all classes unanimously rejected the plan of arrangement and no acceptances could be found. In fact, in the *Meyer* case there was no attempt made to utilize § 461 of the Bankruptcy Act

[32]"Everyone who takes a mortgage, or a deed of trust intended as a mortgage, takes it subject to the contingency that proceedings in bankruptcy against his mortgagor may deprive him of the specific remedy which is provided for in his contract." *In re Jersey Island Packing Company*, 138 F. 625, 627 (CA 9, 1905).

[33]*Meyer v. Rowen*, 195 F.2d 263 (1952), and *In re Herweg*, 119 F.2d 941 (1941).

[34]*In re Colonial Realty Inv. Co.*, 516 F.2d 154; *Gonzalez Hernandez v. Borgos*, 343 F.2d 802; *Owners of "S.W. 8" Real Estate v. McQuaid*, 513 F.2d 558; *In re Dick*, 296 F.2d 912; *Ellis v. Yumen*, 324 F. Supp. 1314; *In re Pittsburgh-Duquesne Dev. Co.*, 327 F. Supp. 1194, reversed 482 F.2d 243; *Sumida v. Yumen*, 409 F.2d 654, appeal after remand 444 F.2d 1281, cert. den'd. 405 US 964, rehearing den'd. 405 US 1048; *Ellis v. J-R-M Corp.*, 324 F. Supp. 768; *Crosby v. Mills*, 413 F.2d 1273; *Bushey v. Peters*, 345 F.2d 178; *Sayers v. Forsyth Building Corp.*, 417 F.2d 65; *In re Decker*, 465 F.2d 294; *In re Rubicon, Ltd.*, 331 US 858, rehearing den'd. 375 US 936; *Perry v. Commerce Loan Co.*, 383 US 392, rehearing den'd. 384 US 934; *Acme Tool, Inc. v. Flesher*, 309 F.2d 636; *Taylor v. Wood*, 458 F.2d 15; *In re Pawling*, 415 F.2d 1212; *In re Johnson*, 418 F.2d 246, cert. den'd. 96 S. Ct. 191; *Posi-seal Intern., Inc. v. Chipperfield*, 457 F.2d 237.

[35]*Keyser v. MacAdam*, 117 F.2d 232; *In re Hamburger*, 117 F.2d 932; *In re Herweg*, 119 F.2d 941; *Meyer v. Rowen*, 195 F.2d 263; *Raider v. Boyd*, 267 F.2d 911.

[36]"Plan" and "Claims" in § 216(7) are substituted respectively for "Arrangement" and "Debts" in § 461(11).

[37]*In re Franklin Garden Apartments, Inc.*, 124 F.2d 451; *Country Life Apartments, Inc. v. Buckley*, 145 F.2d 935; *Scherk v. Newton*, 152 F.2d 747; *National City Bank of N.Y. v. O'Connell*, 155 F.2d 329; *Eddy v. Prudence Bonds Corp.*, 165 F.2d 157; *In the matter of Frank Fehr Brewing Co.*, 268 F.2d 170; *U.S. v. Key Ind.*, 397 US 322; *White v. Penelas Mining Co.*, 105 F.2d 726; *Texas Hotel Securities Corp. v. Waco Dev. Co.*, 87 F.2d 395, cert. den'd. 300 US 679, rehearing den'd. 301 US 713; *In re East Boston Coal Co.*, 30 F. Supp. 811; *In re Englander Spring Bed Co.*, 17 F. Supp. 15, aff'd. 86 F.2d 998; *In re Continental Vending Machine Corp.*, 517 F.2d 997; *In re Northeast Corp.*, 379 F. Supp. 1084.

to deal with non-assenting classes, and the plan of arrangement was rejected by the court on numerous grounds which had nothing to do whatsoever with § 461.[38]

The other cases cited by the Class I creditors in support of their argument[39] also involve other aspects of the plans which did not comply with the Bankruptcy Act. That is not the case here, because every class of creditors accepted the arrangement at the hearing on confirmation except the Class I creditors, and no objection was raised at that hearing to the Plan of Arrangement except for the objections of the Class I creditors as discussed herein. Under these circumstances, the cases cited by the Class I creditors in their brief do not require the results for which they argue, and the Court concludes that since all classes of creditors other than them have voted affirmatively for the Plan, § 461(11) can be used to deal with the Class I creditors as a nonassenting class.[40]

In the general dearth of authority of judicial opinions construing Chapter XII of the Bankruptcy Act, and, particularly, the application of § 461(11)(c), the decision of the United States Court of Appeals for the Tenth Circuit in *Rader v. Boyd*, 267 F.2d 911 (1959), supports the Court's construction of this Section of the Bankruptcy Act. In that Chapter XII proceeding, the debtor proposed a plan of arrangement which was not accepted by a secured creditor in circumstances similar to this case. The principal difference was that the fair value of the creditor's security in *Rader* was greater than the debt owed the creditor and the plan of arrangement proposed to pay the creditor less than the fair value of the security. The court held that such an application of § 461(11)(c) would not provide adequate protection for that creditor, and in considering this point, the court said:

> "The evidence of the sponsors of the Arrangement is that the property is worth far more than the debts due Boyd. In such *circumstances* Boyd is entitled to be paid and the proposed Arrangement does not adequately protect him. The requirements of § 461(11) for 'adequate protection' mean that *when the value of the security is greater than the debt*, the protection afforded by an Arrangement must be completely compensatory."
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> *Rader v. Boyd, supra*, at p. 913 [Emphasis added.]

The above quoted language clearly implies that where the value of the security is less than the debt, adequate protection would be afforded by a payment in the amount of the value of the security and not the amount of the debt. Otherwise,

[38]See *Meyer v. Rowen, supra*, at p. 265.

[39]*In re Potts*, 142 F.2d 883 (CA 6, 1944); *Preas v. Kirkpatrick and Burks*, 115 F.2d 802 (CA 6, 1940); and *In re Taylor v. Wood*, 457 F.2d 15 (CA 9, 1972).

[40]The court does not view the treatment which has been afforded Class I creditors thus far in this proceeding, and the treatment which will be afforded the Class I creditors by a proper application of § 461(11)(c), to be inequitable. (By order of this Court dated March 20, 1976, the gross rent receipts less necessary operating expenses are paid to the creditor and the Court held that the value of the project had not deteriorated since the filing.) In reorganization proceedings, the courts have clearly recognized that secured creditors, although they may hold the overwhelming majority of the debts in amount and have first priority liens on the debtor's property, may not totally control the proceeding and defeat the plan if they can be treated equitably in the plan or outside the plan. See *Wachovia Bank & Trust Company v. Harris*, 455 F.2d 841 (CA 4, 1972).

the distinction which the court makes in the above quoted language would be useless. As indicated hereinabove, the words of the statute strongly support this construction, and more especially so in light of the amendments thereto eliminating the "fair and equitable rule" from Chapter XII.

The Court concludes, therefore, that Congress intended the provisions of § 461 (11)(c) to be available and applicable to this Debtor as a part of a plan to deal with the nonassenting class of secured creditors, and that a plan which provides for the payment in cash of the appraised value of the debt of the nonassenting class may be confirmed by the Court if the plan is also for the best interest of creditors and is feasible as provided in § 472.

(e) Constitutionality of § 461(11)(c).

The question, perforce, is presented (*Continental Bank v. Rock Island Ry.*, 294 US 648, 667 (1935)), whether an appraisal of the value of the debt and payment of said debt to the secured creditor under § 461(11)(c) is completely compensable and the equivalent of the debt so as to protect the constitutional rights of the creditor guaranteed by the Fifth Amendment to the Constitution.[41]

The Court finds no trial or appellate court decision in point dealing with the constitutionality of § 461(11) or (12); however, some decisions under prior Acts of Congress (allowing appraisal of real property security and payment of cash to satisfy the debt which exceeds the value of the property allowed to be retained by the debtor), shed enough light on this issue to satisfy this Court that § 461 (11)(c) does not exceed the limit allowed by such clause of the Fifth Amendment.

The Frazier-Lemke Act[42] was a temporary emergency farmer relief Act enacted in 1935 during the depths of the Great Depression when foreclosures on farms throughout the United States were rampant. It added subparagraph (s) to § 75 of the Bankruptcy Act which had been added in March, 1933. This first Frazier-Lemke Act (1935), which permitted a farmer to take action to forestall foreclosure proceedings on his farm by secured creditors for up to a period of five years, was declared unconstitutional in 1935.[43]

Whereupon, after said decision, Congress, within three months, enacted in August, 1935 a revised Frazier-Lemke Act to remedy the criticisms of the Supreme Court. Speaking through Justice Brandeis, who wrote both decisions, the Supreme Court approved the second Act, and held[44] that the alteration of several rights in property

[41]The pertinent part of the Fifth Amendment reads as follows: "No person shall be . . . deprived of life, liberty or property without due process of law; nor shall private property be taken for public use without just compensation."

"[T]he Fifth Amendment commands that however great the nation's need, private property shall not be thus taken even for a wholly public use without just compensation." *Joint Stock Land Bank v. Radford*, 295 US 555 (1935) at p. 602.

[42]48 Stat. 1289.

[43]*Louisville Joint Stock Land Bank v. Radford*, 295 US 555 (1935). The Court held that while some property rights of secured creditors can be constitutionally altered or modified, the Act infringed upon *too many* of the rights of secured creditors so as to violate the due process clause of the Fifth Amendment of the Constitution which prohibits the taking of property without due process of law.

[44]*Wright v. Vinton Mountain Trust Bank*, 300 US 440, 81 L ed 736, 57 S. Ct. 556.

of secured creditors, including forestalling secured creditors for up to three years from foreclosure for delinquency under the debt in order to permit a farmer-owner to continue to occupy the premises, and to pay the secured creditor the value of the property as determined by appraisal to "redeem" the property from the debt,[45] did not offend the Fifth Amendment.

It should be noted in assessing the significance of these two decisions, that Justice Brandeis in both the original *Radford* opinion, and in the *Vinton Bank* opinion emphasized that one constitutional infirmity of the original Frazier-Lemke Act lay in its application to mortgages given prior to the enactment of the Act in that it effected a substantial impairment of the mortgagee's security as it existed prior to the Act.[46] In this case, however, such infirmity cannot be charged because there have been no substantial changes in Chapter XII of the Bankruptcy Act from the time the Class I creditors obtained their security interest in the Debtor's property, and the Court concludes that these creditors took their security subject to the provisions of the Bankruptcy Act in effect both then and now.

Three years thereafter, in June, 1938, the Chandler Act[47] substantially revised the Bankruptcy Act of 1898, especially in the area of reorganizations, compositions and arrangements, amid the economic, social, and political pressures of that period of great stress during the so-called Great Depression. In the background of the experiences of the years since 1898, and especially since 1930, Congress included in Chapter XII much of the philosophy of the second "Constitutional" Frazier-Lemke Act and other depression oriented farmer relief legislative experiments. Understanding such origins, one can see why Chapter XII applies only to individuals, partnerships, and other unincorporated entities, and does not apply to corporations. Yet, Chapter XII, accommodates more modern entities, such as the Debtor here, which participated in the development of real properties during the past few years.

Upon another contest of the second Frazier-Lemke Act, the *Wright v. Union Central Life Insurance Company* case[48] held that the appraisal provisions of the amended § 75(s) was not only constitutional, but mandatory, and that the "right" of the secured creditor to a public sale was limited to situations where the debtor had *failed* to pay the appraised price. It is significant to note that the *Union Central* case involved a situation where a farmer-debtor owed $15,903.68 to his secured creditor, and the property which he sought to "redeem" was valued at $6,000.00. In upholding the right of the farmer to pay this appraised amount to redeem his property from the security interest of his creditor, Justice Douglas, in commenting on the constitutional rights of the secured creditor, stated:

[45]The creditor had the election to have the property reappraised at the time the farmer decided to exercise his option to pay the debt within said three years.

[46]See *Louisville Joint Land Bank v. Radford, supra*, at pp. 589 and 590, and *Wright v. Vinton Mountain Trust Bank, supra*, at pp. 456 and 457.

[47]Act of June 24, 1938, Chap. 575, 52 Stat. 840-940.

[48]311 US 273 (1940). The holding is discussed at length in 5 *Collier on Bankruptcy* § 77.17 (14th Ed.). The decision is significant in contrast to the apparent holdings in the *Radford* and *Vinton Bank* cases that a judicial sale is a necessity.

"We think that the denial of an opportunity for the debtor to redeem at the value fixed by the court [i.e., appraisal] before ordering a public sale was error."[49]

". . . Safeguards were provided [in § 75(s)] to protect the rights of secured creditors, throughout the proceedings to the extent of the value of the property . . . ." "There is no constitutional claim of the creditor to more than that."[50]

The remedy of judicial sale provided for by § 75(s) of the Bankruptcy Act was "denied the creditor only in case he has been paid the full amount of whatever he can constitutionally claim". *Id.*, p. 279.

The *Union Central* case makes it clear that the value of the property (i.e., appraisal by the court) is the full amount the secured creditor can constitutionally claim. A secured creditor is "constitutionally" entitled to payment of nothing more than the actual value of the security. Here, the Debtor may "constitutionally" redeem its property from the debt of the secured creditor by paying to it the actual value of the apartment project.

These decisions establish that there is no magic in a judicial sale,[51] and that a judicial sale is not the only method of determining value of property, and that any reasonable method of ascertaining such an appraisal is constitutionally permissible, so long as the creditor is accorded procedural due process and receives the value of the debt.[52] In addition to these cases, the Court also notes the case of *Reconstruction Finance Corporation v. Denver & Rio Grande W. R. Company*, 328 US 496 (1946), where the Supreme Court sustained the "cram down" provision of § 77 of the Bankruptcy Act, which authorizes a railroad reorganization court to confirm a plan despite its rejection by creditors. In so doing, the Court,

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[49]"This Act provided a procedure to effectuate a broad program of rehabilitation of distressed farmers faced with the disaster of forced sales and an oppressive burden of debt." *Wright v. Union Central, supra,* p. 278.

[50]*Union Central Life Insurance Company, supra,* at p. 278. See also Patrick Murphy, "Secured Creditors in Chapter Proceedings," *The Business Lawyer,* Vol. 30, 1974, p. 25 where Murphy comments that this is the "clearest statement of the right of the secured creditor; namely to receive the value of the collateral and to have the right protected throughout the proceeding."

[51]*Louisville Joint Stock Land Bank v. Radford,* 295 US 555, (1935) *Wright v. Vinton Mountain Trust Bank,* 300 US 400 (1936) and *Wright v. Union Central,* 311 US 273 (1940). See also fn 18 and 19 herein.

[52]*In the matter of Witherbee Court Corp.,* 88 F.2d 251 (CA 2, 1937): "Any reasonable method of ascertainment [of value] as with sale is permissible; the essential thing is to give the mortgagee the benefit of that value. Reasonable methods of ascertaining it are obviously open to Congress without infringing on the Fifth Amendment." *Collier, supra,* p. 485 fn 23.

If a method is provided for judicial ascertainment of the value of the property affected, it would seem that all constitutional requirements are fulfilled. *Collier, supra,* § 10.16, p. 487, fn 28. "As to a dissenting class of senior creditors, it seems that there is no constitutional right to insist on a judicial sale, if there is a provision for realization of what the class can constitutionally claim 'as the value of its claim' ". *Collier, supra,* Art. X, § 10.16, p. 448.

In the several cases dealing with the Frazier-Lemke Act (§ 75(s) of the Bankruptcy Act), the court spoke to the due process clause of the Fifth Amendment and did not differentiate due process and just compensation as separate considerations in the Fifth Amendment. See also *Patrick Murphy, supra,* fn 50.

in a passage footnoted by a citation to the *Wright v. Union Central* case, *supra,* stated as follows:

"We think that the provisions for confirmation by the courts over the creditors' objection are within the Bankruptcy powers of Congress. Those powers are adequate to eliminate claims by administrative valuations with judicial review and they are adequate to require creditors to acquiesce in a fair adjustment of their claims, so long as the creditor gets all the value of his lien and his share of any free assets."

Reconstruction Finance Corp. v. Denver & Rio Grande G. W. R. Co., supra, at p. 533.

See also the *Regional Rail Reorganization Act* cases, 419 US 102 (1974), in which the Supreme Court upheld a similar "cram down" provision in the Rail Act by observing "There are, therefore, ample adequate '[s]afeguards . . . to protect the rights of secured creditors . . . to the extent of the value of the property' ", citing *Wright v. Union Central, supra,* and further citing *Reconstruction Finance Corporation v. Denver R. G. W. R. Co., supra.* See *Regional Rail Reorganization Act* cases, *supra,* pp. 153 and 154.

Those decisions dealing with § 75(s) (Frazier-Lemke Act), which was the statutory genesis of Chapter XII, together with the other Supreme Court cases cited hereinabove, establish that, constitutionally, a secured creditor is entitled to receive no more than the appraised value of the secured property as just compensation for the loss of the property and the satisfaction of its security interest. Moreover, where, as here, the debtor has been exculpated from personal liability for said debt through contractual arrangements with the secured creditor, the secured creditor has no constitutional claim to share in any "free assets" of the debtor, and constitutionally, can be required to accept the appraised value of the property in cancellation of its debt. *Collier* emphasizes that the lesson from these decisions is that "the dissenting class must be given 'completely compensatory" treatment and the 'indubitable equivalence' of the rights surrendered".[53] Although this language is somewhat colored by the continued existence of the "fair and equitable" rule applicable in Chapter X cases, and inapplicable to Chapter XII cases, the Court concludes, by analogy, that § 461(11)(c), and the Plan herein proposed, does just that, and is in the best interest of creditors and feasible.

Hence, this Court concludes that there is ample authority to support the constitutionality of § 461(11)(c).[54] Furthermore, this Court concludes that as applied to the facts of the case at bar, where the dissenting secured creditors have, by contractual agreement, exculpated the Debtor and all persons associated with it from personal liability for any part of the debt, Section 461(11)(c) may be constitutionally applied to extinguish the debt of the dissenting secured creditors, and a Plan of Arrangement confirmed in spite of such dissenting class, so long as

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[53]*Collier, supra,* Chapt. X ¶ 10.16, p. 448, fn 33 (14th Ed.).

[54]One commentator stated far earlier that, "Since the decision of the Supreme Court in *Continental Ill. Nat. Bank & Trust Co. v. Chicago R. I. & Pac. Ry.,* 294 US 648 (1935), there can be little doubt that Section 77B in its general aspects is constitutional as an exercise of the bankruptcy power." *46 The Yale Law Journal,* 116, 120, *supra,* fn 18 and 20 herein.

the dissenting class of creditors is compensated by the payment in cash of the value of the debt; i.e., the value of the secured property.

(c) **Valuation of the Secured Property.**

The question of the fair value of the property which is security for the debt owed the Class I creditors is properly before the Court. During the prior hearings conducted by the Court on a complaint to lift the injunction against foreclosure brought by the Class I creditors, a witness for the Class I creditors testified that the value of the property in question is approximately $850,000.00. Other testimony of the Class I creditors put the value at approximately $1,000,000.00. On the other hand, the plan of the Debtor proposes to pay in cash to the creditors of Class I the amount of $1,200,000.00.

Although the Court would perhaps be justified in utilizing this evidence to establish the value of the property for the purposes of § 461(11)(c), in all fairness to the parties, the Court observes that neither the presentation of evidence in the reclamation proceeding nor the proposal of the Debtor in its Plan of Arrangement were put forth in contemplation of the requirements of § 461(11)(c). Furthermore, to insure that the Class I creditors receive the procedural due process to which they are entitled in the determination of the value of their debt, this Court concludes that a hearing specifically on the question of the value of the property for use in fixing the amount required to be paid to the creditor under § 461(11)(c) is appropriate.

It is this ultimate question which is the most difficult to determine. That is, what is the "value" which is anticipated by § 461(11)(c)?[55]

Accordingly, the Court will afford to the Class I creditors and the debtor an opportunity to present to the Court any evidence they desire as to the value of the property and what payment in cash by the debtor to the creditors will offer adequate protection and be completely compensatory and just compensation for the property which is security for the debt of the Class I creditors.

IV. CONCLUSION.

The Court requests briefs from the Class I creditors and the Debtor within 30 days from this date as to what method of valuation must be applied under § 461(11)(c) to determine value in the case sub judice. Further, the Class I creditors and the Debtor are hereby directed to present evidence as to the value of the real property securing the debt of the Class I creditors, and to show cause before this Court on the 30th day of November, 1976, at 11:00 o'clock A.M. in Room 546, United States Courthouse, 56 Forsyth Street, Atlanta, Georgia, what amount the Debtor must pay to the Class I creditors in cash for the property which is security for the indebtedness owed the Class I creditors in order to provide adequate protection to the Class I creditors under § 461(11)(c) and to be completely compensatory and just compensation to the Class I creditors. At such

[55] *Murphy, supra,* page 25, (fn 50 herein). See also *Collier,* (14th Ed.), Vol. 6A, paragraph 10.16, page 488. See also discussions re valuation before the U.S. Senate Committee on the Judiciary, Subcommittee on Improvements in Judicial Machinery, Hearings on *The Bankruptcy Reform Act,* Part II, p. 371-374 (U.S. Government Printing Office).

time and place, the Court will receive any evidence in the form of appraisals, or otherwise, which the Class I creditors or the Debtor may desire to present to the Court. Thereafter, the Court will enter an order establishing the value of the property and ordering a payment to the Class I creditors of said amount in cash as a condition to the confirmation and implementation of the Plan of Arrangement.

SO ORDERED, this the 14th day of October, 1976, at Atlanta, Georgia.

/s/ WILLIAM L. NORTON, JR.
William L. Norton, Jr.
United States Bankruptcy Judge

APPENDIX L

APPENDIX "L"

NAME	DATE FILED	CASE NUMBER
1975		
Bolton Road Medical Center	1/6/75	B75-38A
Bolton West Ltd.	1/7/75	B75-39A
Crestway Properties	1/7/75	B75-50A
Consolidated Motor Inns	1/23/75	B75-296A
Pine Ridge	3/3/75	B75-870A
Helmwood Apts. Phase I & II	5/6/75	B75-1763A
Mendel Roman, Jr.	6/2/75	B75-2095A
Peyton Place Apts. Ltd.	6/2/75	B75-2097A
Peyton Towers Apts. Ltd.	6/2/75	B75-2096A
Atlanta Lane Investments	6/8/75	B75-2118A
H. Dean Bevedon	8/4/75	B75-2756A
Lake Colony	8/26/75	B75-2971A
John Allen Kelley	10/5/75	B75-3435A
Colony Square	10/16/75	B75-3523A
Westminster Club Apts., Dalton	11/3/75	B75-3757A
Tinsley Hill Village	11/3/75	B75-3758
Mountain View Apts.	12/2/75	B75-4079A
Executive Townhouse Apts., Ltd.	12/31/75	B75-4375A
Pine Gate Ass.	12/23/75	B75-4345
1/1/76 - 7/1/76		
Norma Mulligan	1/6/76	B76-32A
James David Mulligan	1/6/76	B76-31A
Athens History Village	2/25/76	B76-630A
Nob Hill Apts.	3/15/76	B76-864A
James Linwood Bentley	5/4/76	B76-1435A
Peachtree North Apts.	5/25/76	B76-1690A

NAME	DATE FILED	CASE NUMBER
Juliet Dowling	5/28/76	B76-1739A
Ashmore-Paces Ferry Property	6/1/76	B76-1741A
Woodlake Apts.	6/2/76	B76-1769A
7/1/76 - 11/1/76		
Arlington III Associates	7/2/76	B76-2068A
Belvedere Properties	7/2/76	B76-2056A
Thomas E. Cotton	7/26/76	B76-2311A
B & B Properties	8/2/76	
Clayton A. West	8/2/76	B76-2375A
Montgomery Motel Investors	9/29/76	B76-2915A
Shallowford Downs Apts.	10/1/76	B76-2957A
Spanish Mansion Ass.	10/4/76	B76-2989A
Daron Ltd.	10/4/76	B76-2987A
Betty Rainwater Stephens	10/5/76	B76-2991A
Francis Ashworth Norris		B76-1733A
St. Simons Properties	10/28/76	B76-3220A
Peachtree Trace Apts.	11/1/76	B76-3251A
Copland Village Ass.	11/1 76	B76-3266A
Kingston Ltd.	11/1/76	B76-3251A